



GOVERNMENT OF PUERTO RICO

PUERTO RICO PUBLIC-PRIVATE PARTNERSHIPS AUTHORITY

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October 4, 2021

By Email

Honorable Raúl Grijalva
Chair
Committee on Natural Resources
U.S. House of Representatives
Washington, DC 20515

Written Statement from the Puerto Rico Public-Private Partnerships Authority in relation to the Full Committee Oversight Hearing to be held on October 6, 2021, titled "PREPA Post Implementation of the LUMA Transmission and Distribution Contract"

Introduction

Chairman Grijalva, Ranking Member McMorris Rodgers and Committee Members, thank you for the opportunity to appear before you today. My name is Fermín Fontanés Gómez and I am the Executive Director of the Puerto Rico Public Private Partnership Authority (the "P3 Authority").

The P3 Authority is a public corporation of the Government of Puerto Rico created pursuant to the Public-Private Partnership Authority Act, Act No. 29-2009 (as amended, "Act 29"), and is the government entity charged with transforming Puerto Rico's electrical grid by securing private sector partners to improve power generation, transmission, and distribution for Puerto Rico. As Executive Director of the P3 Authority, I am leading the efforts related to the transformation, and I recently oversaw the process that resulted in the handover of operations of the Puerto Rico Electric Power Authority's ("PREPA") transmission and distribution system to LUMA Energy LLC ("LUMA" or the "Operator"). Under the agreement between the P3 Authority, PREPA and LUMA ("the O&M Agreement"), LUMA will operate, maintain, and modernize Puerto Rico's transmission and distribution for a 15-year term.

As you are aware, Puerto Rico's electrical system faces severe challenges as a result of years of underfunding, lack of maintenance and disrepair, the devastation caused by hurricanes Irma and Maria, and a series of earthquakes that struck Puerto Rico in December 2019 and January 2020. The transformation process has been further delayed by strict shelter-in-place measures and other restrictions to prevent the spread of COVID-19.

My testimony today will address the government framework for oversight of the transformation process, and will cover the following five topics: (i) the regulatory background underlying the whole transformation process; (ii) the delineation of responsibilities between the government agencies tasked with effectuating the transaction for the transformation of the transmission and distribution system and the Operator; (iii) the status of the proposed reorganization of PREPA, and (iv) the next steps in the transformation of Puerto Rico's electrical grid.

i. Regulatory Framework

The regulatory framework underlying the PREPA transformation rests on three main pillars—the Puerto Rico Electric Power System Transformation Act, Act No. 120-2018 (as amended, "Act 120"), the Puerto Rico Energy Public Policy Act, Act No. 17-2019 ("Act 17"), and the Puerto Rico Transformation and RELIEF Act, Act No. 57-2014 (as amended, "Act 57").

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The Government enacted Act 120 with the objective of transforming Puerto Rico's electric system into one that is modern, sustainable, reliable, efficient, cost-effective and resilient to natural disaster. Further, to address the Legislative Assembly's concern that the Commonwealth's electric power and generation and distribution system was obsolete and hindered opportunities for economic development, Act 17 was enacted requiring PREPA to delegate or transfer operation of the electric power generation, transmission and distribution, commercialization, and operation systems through contracts awarded and executed pursuant to Act 120 and Act 29, all to be done within certain specific milestones.

Created pursuant to Act 57, the Puerto Rico Energy Bureau (the "PREB") is the government agency charged with regulating, overseeing and ensuring compliance with the public policy on energy of the Commonwealth of Puerto Rico. The PREB has served, and continues to serve, an important function in the transformation of PREPA, including the approval of the energy compliance certificate assuring that the O&M Agreement is consistent with Puerto Rico's energy public policy.

ii. Delineation of Responsibilities Among the Relevant Parties

The parties to the O&M Agreement specifically allocated responsibilities among various Government agencies as required by the underlying regulatory framework. Specifically:

- the P3 Authority is charged with overseeing the Operator’s and PREPA’s compliance with the terms of the O&M Agreement;
- the PREB is responsible for regulating, overseeing, and ensuring the Operator’s compliance with applicable law and public policy on energy. As the Island’s independent regulator for the energy sector, the PREB oversees all operational and technical aspects of LUMA’s performance as operator of the transmission and distribution system; and
- PREPA continues to own the transmission & distribution system and is also required to reasonably cooperate with the Operator so that it can perform its obligations under the O&M Agreement.

Operations	PREPA	LUMA	P3A	PREB
Title / Ownership of T&D System	✓			
Right of Access	✓	✓	✓	✓
Provision of T&D Services		✓		
Billing and Collection		✓		
Capital Improvements		✓		
Oversight Rights			✓	✓
Employment of Workforce		✓		
Execution / Administration of Contracts & Procurement of Ancillary Services / Subcontracting		✓	✓	
Liaise with Regulator / Other Overseer(s)		✓		
Preparation & Retention of Records		✓		
Auditing Rights		✓	✓	✓
Maintenance of Insurance Coverage		✓		

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Financial	PREPA	LUMA	P3A	PREB
Formulation and Submission of Budgets		✓		
Approval of Budgets			✓	✓
Federal Funding Sub-grantee	✓			
Federal Funding Eligibility and Process		✓		
Responsible for Financing Capital Projects and Pass-Through Costs (as owner of system revenues)	✓			
Approval of Operator-Owned Capital Improvements				✓
Establishment, Maintenance and Funding of Service Accounts	✓			
Payment of Fixed Fee	✓			
Approval of Incentive Fee			✓	
Payment of Incentive Fee	✓			

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Miscellaneous Contractual Rights	PREPA	LUMA	P3A	PREB
Extend the Initial Term upon Mutual Agreement	✓	✓	✓	
Rights to Terminate the Agreement upon Event of Default		✓	✓	
Rights to Indemnity	✓	✓	✓	
Assignment Rights	✓	✓		
Waivers		✓	✓	
Consent Required for Amendment	✓	✓	✓	✓

a. Role of the Puerto Rico Public-Private Partnerships Authority

The P3 Authority is charged with overseeing Operator's compliance with the terms of the O&M Agreement. As the government agency responsible for overseeing the implementation of all public-private partnerships, the P3 Authority is committed to the success of the project, and fully focused on exercising its contractual oversight functions to achieve the Government's goals.

During the transition period leading to LUMA formally taking over the operation of the transmission and distribution system, the P3 Authority played a pivotal role in ensuring that the Operator was able to begin operation of the transmission and distribution system within the agreed timeframe. The P3 Authority was responsible for assisting in preparing, reviewing and/or approving the System Operation Principles, a System Remediation Plan, Performance Metrics, Initial Budgets, and Procurement Manuals, among others. The P3 Authority reviewed and commented on various drafts of these operating plans, which were required for handover, and participated in multiple working groups with the Operator to refine such plans. In addition, the P3 Authority oversaw the development and implementation of protocols for the review and validation of the Operator's invoices during the front-end transition period.

4 Throughout the term of the O&M Agreement, the P3 Authority is charged with: (i) reviewing and approving the Operator's annual budgets as well as any incentive fee payable to LUMA for achieving certain performance metrics; (ii) exercising oversight in relation to the Operator's compliance with budgets and its performance of its obligations under the contract; and (iii) cooperating with the Operator in its efforts to obtain and effectuate any required government approvals. In order to ensure that the P3 Authority is able to properly execute its mandate and contractual obligations, the Operator is required to deliver monthly reports for the P3 Authority's review. Finally, the P3 Authority holds regular meetings and proactively engages in communication with LUMA in order to discuss matter pertaining to day -to- day execution of the O&M Agreement.

b. Role of the Puerto Rico Energy Bureau

As the independent regulator of the energy system, the PREB has the ultimate responsibility to regulate, monitor, and enforce the energy public policy of the Government. As part of its statutory mandate, the PREB is charged with ensuring that electric service in the Commonwealth of Puerto Rico is safe, reliable, and affordable. In accordance with the regulatory framework established by Act 120, the PREB and the P3 Authority collaborate in supervising LUMA's performance of the O&M Agreement. In addition, the P3 Authority and

the PREB, together with PREPA, continue to work on a work plan to oversee the transaction and guarantee the optimum use of the resources of each entity without unnecessary duplicity or overlapping. As such, the PREB has been tasked with overseeing all technical and operational aspects of LUMA's performance under the O&M Agreement.

As part of its technical oversight functions, the PREB issued a Resolution and Order of May 21, 2021, directing the Operator to prepare quarterly reports with respect to certain performance metrics, including customer service metrics, customer average interruption duration, operational and capital expenses, and certain generation metrics. As further explained below, the first quarterly report covering the period from June 2021 to August 2021 was recently filed with the PREB on September 20th.

Among other responsibilities, PREB has the statutory responsibility to oversee rates charged to consumers. The O&M Agreement specifically states that nothing in the contract is intended to impair or restrict the PREB's right to approve final rates and charges to customers in accordance with applicable law. Therefore, the Operator is subject to regulatory oversight by the PREB and cannot increase rates without PREB's approval. No rate increases are contemplated in the Operator's Initial Budget approved by the PREB for 2022-2024.

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c. Role of the Puerto Rico Electric Power Authority

As of today, PREPA has two distinct roles with respect to Puerto Rico's electric energy system: (i) it is the owner of the transmission and distribution system and, as such, is charged with cooperating with the Operator in its operation and management of the transmission and distribution system; and (ii) it is the owner and operator of the legacy base-load generation plants and gas turbine peaking plants located throughout the island of Puerto Rico.

Pending the completion of the procurement process to delegate the operation and maintenance functions of these generation facilities, PREPA remains responsible for operating the same to generate the electricity that is then transmitted and distributed by the Operator to the people of Puerto Rico.

d. Role of the Private Operator

As required by law, the P3 Authority conducted a procurement process that led to the signing of the O&M Agreement in June 2020, and then oversaw a one year-long transition of operations to LUMA. The transition allowed the parties to prepare for the Operator's takeover of the transmission and distribution system by (i) developing the requisite operating plans, performance metrics, procedures and policies needed for a successful transaction; (ii) hiring

employees to operate the transmission and distribution system; (iii) allowing the Operator to establish a presence on the Island; and (iv) refining the arrangements between LUMA as operator of the transmission and distribution system and PREPA as operator of the electrical generation facilities.

LUMA formally took over the operation of the transmission and distribution system on June 1, 2021. As the operator, LUMA is responsible for the day-to-day operation of the transmission and distribution system, which includes, among other things: (i) electric transmission, distribution and load servicing; (ii) asset management and maintenance; (iii) public and employee safety; (iv) managing and administering Federal funds; (v) human resources; (vi) information technology; (vii) customer services and communicating with the public; (viii) billing and collection; (ix) system planning and operations; (x) implementation and planning of capital improvements; (xi) accounting and financial services; (xii) communicating with, and appearing before, the PREB; (xiii) preparation of the Integrated Resource Plan; (xiv) emergency response; and (xv) communications with the Government, community and the media.

LUMA's first Quarterly Performance Metrics Report filed with the PREB includes data collected by the Operator for the first three months since it commenced operation of the transmission and distribution system on June 1st. The report includes an update on both transmission and distribution metrics and those that involve PREPA's generation using data that the Operator received from PREPA. Highlights from the report as well as trends over the initial three-month period are as follows:

Customer Service-

- the percentage of calls answered improved substantially from 28% to 54% in comparison to PREPA's historical Fiscal Year 2020 data (used as baseline).
- the average wait time to answer calls improved substantially from approximately 26 minutes to approximately 9 minutes in comparison with PREPA's baseline.

T&D Reliability- The initial operating months had significant outages throughout all regions as the Operator worked to transition operations. The August data reflected the significant lack of PREPA's generation resulting in rotating load shedding by the Operator. With regards to specific indicators, the report shows as follows:

- SAIDI (System Average Interruption Duration Index) decreased by 85 minutes. This is still worse than both PREPA's baseline and the benchmark set by PREB in its May 2021 Resolution and Order.

- SAIFI (System Average Interruption Frequency Index) slightly increased. This is still better than both PREPA's baseline and the benchmark set by PREB in its May 2021 Resolution and Order.
- CAIDI (Customer Average Interruption Duration Index) overall customer average interruption time improved, although still worse than both PREPA's baseline and the benchmark set by PREB in its May 2021 Resolution and Order.

Human Resources-

- While absenteeism over the initial 3-month period of June-August increased from 1.1% to 1.9%, it is significantly better than PREPA's baseline of 13.1%. It is also better than the benchmark of 2.4% set by PREB in its May 2021 Resolution and Order.
- The OSHA Total Recordable Incident Rate ("TRIR") worsened during the initial period with injuries reported in August being 8, which was up from 3 in June 2021. LUMA's August TRIR of 2.9% is slightly worse than PREB's benchmark of 2.3% but better than PREPA's baseline of 6.4%.

Power Generation-

- Power plant unit availability worsened by 17% from June to August for the larger base load power plant units.
- Forced Outage Hours increased by over 20% in August versus June 2021.
- The lack of generation/resource adequacy situation led to island-wide rotating load shedding in August and into September. The lack of base load generation also led to operating with the peakers units, which are less efficient and also resulted in fuel cost (\$74 million dollars over projections)

As noted above, in the four months since LUMA began performance under the O&M Agreement, outages continue to be a problem and, in some cases, appear to have worsened. However, during each outage, the P3 Authority has been in constant communication with PREPA and the Operator to seek explanations and facilitate dialogue to remedy the situation as quickly and efficiently as possible. Communication with all parties has been effective and has led to better alignment and delineation of corrective actions.

Also, it is important to point out that the operation and maintenance of the base-load generation plants and gas turbine peaking plants located throughout the island of Puerto Rico remain the responsibility of PREPA. Although the Operator is responsible for cooperating with the generators of electric energy, LUMA is not responsible for any of the operation, repair,

replacement, maintenance or improvement of the legacy electrical generating facilities.

iii. PREPA Reorganization

As part of the transformation process, PREPA is currently undergoing a reorganization with the view toward creating two new subsidiaries—GridCo and GenCo (the “PREPA Reorganization”). Upon completion of the PREPA Reorganization, ownership of PREPA’s transmission and distribution system will be transferred to GridCo and ownership of PREPA’s Legacy Generation Assets will be transferred to GenCo. One of the goals of the PREPA Reorganization is to comply with the public policy mandated in Act 17 which provides for the unbundling of Puerto Rico’s electrical system, the incorporation of the private sector in the operation of assets and the rendering of electric power services so to allow for the elimination of interventions fueled by party politics.

iv. Next Steps in the PREPA’s Transformation – Procurement of Generation Operator

The next step in the transformation of PREPA is the procurement of one or more private operators to assume the operation and maintenance functions of Puerto Rico’s legacy electrical generation facilities, as required by Act 17.

14 Following that mandate, the P3 Authority commenced a procurement process, which purpose is to delegate the operation and maintenance functions of these facilities. The currently ongoing procurement process began with the launch of a request for qualifications to which fifteen private parties responded. In consultation with its financial, technical and legal advisors, the P3 Authority evaluated the statements of qualifications received from those private parties and submitted its analyses to the partnership committee established to oversee the process. The partnership committee short-listed eight private parties with best-in-class expertise and experience to participate in the request for proposals (“RFP”) phase.

On November 10, 2020, the P3 Authority launched the RFP phase with the issuance of the RFPs to the eight qualified parties. Since the issuance of the RFP, this process has advanced steadily. Currently, interested parties are conducting site visits and continuing to conduct due diligence and engage on the draft contract negotiations.

Upon award of the generation contract, the selected generation operator(s) and LUMA will work in parallel to operate Puerto Rico’s electric energy system.

Both the Operator and the generation operator(s) to be selected as part of this procurement process are and will be legally bound to comply with PREB’s

regulations and orders and with the applicable legal framework that regulates the energy industry in Puerto Rico, including the mandates of Act 17 for the integration of renewable energy into the grid. Renewable energy objectives are one of many goals set by the Government to achieve the modernization of Puerto Rico's electric system. The transformation is a multi-step process that will be accomplished over multiple years. The O&M Agreement is but the first step in this transformation and is aimed at repairing, remediating and strengthening the transmission and distribution system. Without that, Puerto Rico will never be able to develop a fully resilient energy infrastructure. The Government of Puerto Rico is committed to ensuring the creation on a sustainable electric grid and creating the transmission and distribution system more capable to manage and incorporate cleaner sources of energy.

Conclusion

Puerto Rico's electrical system transformation will not be accomplished in the span of four months. However, with the oversight of the P3 Authority, we are confident that the Operator will be able to achieve the goals the parties have set out to accomplish. Like any transition and as was expected, there have been certain challenges. From the moment the new transmission and distribution system operator was announced, naysayers have engaged in a campaign of misinformation aimed at frustrating and derailing the transaction. In addition to this, the Operator inherited a very frail electrical system as a result of years of lack of maintenance, underfunding and disrepair. Everyone knows that transforming Puerto Rico's electric system is not going to happen overnight – it is a process that will take time and effort. It is true that outages continue to affect the residents of Puerto Rico but we must not continue to come up with temporary solutions to a permanent problem, and to that end, the Government of Puerto Rico is committed to ensuring that the Operator addresses the issues faced by the transmission and distribution system and brings it in line with industry standards.

Notwithstanding the challenges faced in the last few months, the Government of Puerto Rico remain confident that the O&M Agreement is an important part of Puerto Rico's transition to a modern, affordable, resilient, and reliable electric energy system that will serve as a driver of economic recovery and growth.

Thank you.


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