

COMMONWEALTH OF PUERTO RICO
PUERTO RICO ENERGY COMMISSION



IN RE: REVIEW OF RATES OF THE
PUERTO RICO POWER AUTHORITY

NO.: CEPR-AP-2015-0001

MATTER: PROVISIONAL RATES

ORDER ESTABLISHING PROVISIONAL RATES

On May 27, 2016 the Puerto Rico Electric Power Authority ("PREPA") filed a *Petition for Approval of (1) Permanent Rates and (2) Temporary Rates*¹ ("Petition") pursuant Act 57-2014 as amended, known as the Puerto Rico Energy Transformation and RELIEF Act ("Act 57-2014") and Act 83 of May 2, 1941, as amended ("Act 83"). This Order addresses the request made pursuant to Section 6A(e) of Act 83, Section 6.25(d) of Act 57-2014 and Section 2.02 of Regulation No. 8720², for a "provisional" rate increase. In its Petition, PREPA proposes a distinct percentage increase to each customer class to recover what it considers to be a deficiency of \$222,256,790 (on an annual basis).³ The deficiency represents part of the difference between the revenue produced by PREPA's current rates and the revenue PREPA says it requires to operate sufficiently.

In this Order, the Puerto Rico Energy Commission ("Commission") **GRANTS** PREPA's petition for provisional rates, as modified by the Commission. The Commission grants this petition in light of PREPA's sensitive financial condition. In doing so, the Commission does not pass judgment on the adequacy or extent of PREPA's efforts to increase efficiency and reduce wasteful operational practices. We will address those issues during the proceeding on permanent rates. Furthermore, the Commission emphasizes that this Order approves only provisional rates. When the Commission sets permanent rates, it has the power to determine whether this provisional rate increase was accurately determined; and, if not, to make adjustments retroactively.

I. INTRODUCTION

Act 57-2014 and Act 83 allow PREPA to request provisional rates, provided such request is made within a petition for rate review filed before the Commission. Section 2.02(E) of Regulation No. 8720 requires PREPA to support its request with pre-filed testimony and other evidence. The Commission has the discretion to perform a

¹ See PREPA's filing on Case No. CEPR-AP-2015-001.

² New Regulation on Rate Filing Requirements for the Puerto Rico Electric Power Authority's First Rate Case ("Regulation No. 8720"),

³ For purposes of brevity, this Order will refer to the amount as \$222 million.

preliminary evaluation to determine if such provisional rates should be established during the period of time needed by the Commission to evaluate PREPA's proposed new rates and up to the date the new rate is implemented.⁴

The provisional rates are temporary in nature, and shall not be in effect for more than sixty (60) days after the final order by the Commission on permanent rates is issued.⁵ If the permanent rates differ from the provisional rates, Act 57-2014 and Act 83 require the Commission to direct PREPA to establish a mechanism to adjust customers' bills retroactively, in order to reconcile any discrepancy between the provisional rate established by the Commission and the rate approved by the Commission in the final order.⁶ Additionally, the Commission may issue any order that it deems fit and/or necessary to modify the provisional rates during its effective term.

II. PROCEDURAL FACTS

The petition for provisional rates was filed along PREPA's formal petition for a permanent rate increase on May 27, 2016. On June 13, 2016, pursuant to Section 6A(c) of Act 83, the Commission issued a *Resolution and Order* where it determined that PREPA's Petition was incomplete and detailed the information the Commission deemed was missing from the initial petition filing.⁷ In such *Resolution and Order* the Commission clearly expressed that the "determination of incompleteness shall not affect the Commission's ability to approve a provisional rate, provided the information included in the Petition is sufficient for the Commission to issue an informed determination with regards to the establishment of a provisional rate."⁸

Pursuant to Act 57-2014 and Act 83, "[w]ithin thirty 30 days after the filling of the rate modification request, the Commission may make, *motu proprio*, or at the request of the Authority, a preliminary evaluation to determine whether the provisional rate should be established."⁹ The approval of any provisional rates falls within the Commission's discretion and is subject to the requirements of Section 2.02 of Regulation No. 8720, which establishes that:

[...] The application for Provisional rates must be clearly marked as such and must include the following elements:

⁴ Section 6A(e), Act 83 of May 2, 1941 and Section 6.25(d), Act 57-2014. Act 57-2014 grants the Commission ample powers to establish, modify or reject any petition for provisional rates filed by PREPA or to set provisional rates without an express request from PREPA, if doing so is in the public interest and will further Act 57-2014's public policy.

⁵ *Id.*

⁶ Section 6A(f), Act 83 of May 2, 1941; Section 6.25(e), Act 57-2014 and Section 2.02(C) of Regulation No. 8720.

⁷ Resolution and Order of June 13, 2016 on Case No. CEPR-AP-2015-001.

⁸ *Id.*

⁹ Section 6A(e) of Act 83 of May 2, 1941, as amended. *See also*, Section 6.25(d) of Act 57-2014, as amended, and Section 2.02 of Regulation No. 8720.

- A) The Provisional rates shall be calculated by applying a specific percentage uniformly to the then-existing base rates, not to any new rate design proposed by PREPA for permanent rates. Such percentage shall be applied to the per-kilowatt hour (kWh) rate and to each other component of the existing base rate structure, including without limitation, the fixed customer charge and any demand charge. The Provisional rate shall not modify the rider that recovers the cost of fuel and purchased power.
- B) It shall demonstrate how the Provisional rates collect the new revenue requirement proposed by PREPA.
- C) It shall include a mechanism for tracking any increase or decrease resulting from the Provisional rates, so as to ensure compliance with Article 6.25(e) of Act 57-2014 and Section 6A(f) of Act 83-1941 (which require PREPA to credit or collect any difference between the Provisional rate and the permanent rate established by the Commission accrued during the term in which the Provisional rate remained in effect).
- D) If PREPA is requesting that the Provisional rate enter into effect prior to the statutory sixty (60) day period, the application for Provisional rate shall include the specific date on which the Provisional rate would go into effect.
- E) It shall include pre filed testimony and exhibits demonstrating the need for the proposed Provisional rates. Such demonstration shall include documentation for the requested revenue requirement and the amount to be recovered in the Provisional rates. Such testimony shall be separate from but may reference, testimony supporting the Application for Permanent Rates.

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On May 4, 2016 PREPA filed a motion seeking a waiver and/or clarification on Section 2.02 of Regulation No. 8720. On May 11, 2016 the Commission issued an Order where it clarified that PREPA should provide, for the Commission's consideration, at least two (2) alternatives for the implementation of provisional rates. One alternative must contemplate the application of a uniform percentage change in base rates across all customer classes and; another alternative shall contemplate the application of a specific percentage change in base rates for each customer class, provided that said percentage change was applied uniformly within each class.¹⁰

After a preliminary review of PREPA's request for provisional rates, on June 16, 2016, the Commission issued an Order requiring PREPA to provide additional information

¹⁰ See Resolution and Order on Case No. CEPR-AP-2015-001 of May 11, 2016. It should be noted that, while the Commission required PREPA to provide at least two (2) alternatives, such a requirement does not limit the Commission's ability and statutory authority to explore additional alternatives which provide an adequate and equitable result.

and clarification on some of the information contained in its Petition. Specifically, the Commission directed PREPA to explain why it sought a provisional rate increase to recover approximately \$222 million in revenue requirement, rather than an increase reflecting its total claimed revenue deficiency of approximately \$725 million, which includes revenues that PREPA was anticipating to collect through the Transition Charge, expected to go into effect later this year.¹¹ The Commission also inquired about the consequences and practical concerns of approving provisional rates designed to recover a portion of PREPA's revenue deficiency, rather than the total revenue deficiency, and to clarify any negative consequence or outcome to PREPA's financial condition should the Commission authorize the provisional rates as requested.¹²

Upon evaluation of PREPA's petition for provisional rates, and its answer to the Commission's request for clarification, the Commission proceeds with its analysis and decision.

III. PREPA'S REQUEST AND RATIONALE

Pursuant to Commission's Order of May 11, 2016, PREPA presented two provisional rates alternatives. The first one was an application of a uniform percentage increase to the existing base rates for all customers. In its evaluation of this alternative, PREPA determined that the necessary increase would be of 20.7 percent for all customer classes. Regarding this proposal, PREPA's witness Mr. Ralph Zarumba expressed in his testimony that he did not recommend a uniform percentage for all customer classes, because applying a uniform percentage increase will result in rates that deviate greatly from PREPA's proposed permanent base rates, which could result in a complicated, expensive and burdensome process at the reconciliation stage.¹³

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The second alternative presented by PREPA was to implement different percentage increases to the existing base rates by tariff class of service, while within each tariff class the same percentage increase will be applied to all components of the base rates. In his testimony, Zarumba conveyed that this was PREPA's preferred approach.¹⁴ According to Zarumba, this alternative establishes a different per-kWh charge for all rate classes, ranging from 0.59 ¢/kWh and 0.60 ¢/kWh for other public authorities and industrial clients, respectively, to 1.45¢/kWh for residential clients, and a 19.62 ¢/kWh increase for public lighting.¹⁵

Finally, in addressing the need for reconciliation (i.e. the retroactive reconciliation of the provisional rates with the permanent rates) as required by Section 6A(f) of Act 83

¹¹ The Commission approved the transition charge calculation methodology on June 21, 2016 on Case No. CEPR-AP-2016-0001.

¹² See Resolution and Order on Case No. CEPR-AP-2015-001 of June 15, 2016.

¹³ Ralph Zarumba Testimony, PREPA Ex. 12.0 at 4.

¹⁴ *Id.*

¹⁵ *Id.* at 5.

and Section 6.25(e) of Act 57-2014, Zarumba explained that such reconciliation will be made in an overall just and reasonable manner in the form of bill credits to current customers and refunds to former clients. Zarumba recommended to perform the reconciliation on a customer class basis without individualized research and back billing in order to avoid difficulties. According to Zarumba's recommendation, refunds or surcharges would be credited or billed, at PREPA's discretion, but subject to Commission's approval, over a period of time not to exceed twelve months, based on the fact that temporary rates will be in effect over a period of several months.¹⁶

In support of its petition for provisional rates, PREPA, through the testimonies of Executive Director Javier Quintana and Chief Restructuring Officer Lisa Donahue, argues that the request for provisional rates is based on PREPA's immediate need for cash flow, which should be addressed before the permanent rates come into effect.¹⁷ They explain that PREPA has a liquidity crisis which threatens its ability to operate, including its ability to purchase fuel to run its power plants.¹⁸ The witnesses explain that the liquidity crisis is reflected in PREPA's "debt obligations of approximately \$9 billion dollars, including approximately \$1.3 billion in principal and interest that will be due on July 1, 2016, under its existing revolving credit lines and power revenue bonds. PREPA has approximately \$550 million in cash, including \$146 million in Government Development Deposits that are subject to a moratorium."¹⁹ To summarize, according to the Petition, PREPA does not have sufficient cash flow to operate and meet its obligations in the near term, before the Petition for permanent rates is reviewed and approved. Those circumstances, the witnesses testified, support the need for an immediate mechanism to manage PREPA's cash flow challenges in the interim period.²⁰

Aggravating the situation, Donahue testifies to the fact that (1) PREPA no longer has access to capital markets on reasonable terms, (2) creditors have not agreed to extend financing in order for PREPA to comply with its financial obligations in July 2016, and (3) PREPA needs to raise revenues immediately to cover operational costs and expenses.²¹ In specific, Donahue states that PREPA faces a funding gap of more than \$700 million as of July 1, 2016, including the need to replenish its self-insurance fund, which helps PREPA be protected against unexpected needs.²²

PREPA also argues that despite its current cash constraints, it has taken substantial measures to reduce its costs by focusing on operational improvements to core business functions.²³ However, the witnesses assert that additional cutbacks on expenditures will

¹⁶ *Id.* at 7.

¹⁷ Verified Petition for Permanent Rates and Provisional rates at 20(34); Javier Quintana Testimony, PREPA Ex. 1.0 at 5, 24 & 29; Lisa Donahue Testimony, PREPA Ex. 10.0 at 3-4.

¹⁸ Ex. 10.0, *supra*, at 3.

¹⁹ Ex. 10.0, *supra*, at 3; *See also* Ex. 1.0 *supra* at 29.

²⁰ Ex. 10.0, *supra*, at 3; Ex. 1.0 *supra* at 24.

²¹ Ex. 10.0, *supra*, at 4.

²² *Id.* at pages 4-6.

²³ Ex. 10.0, *supra*, at 7; Ex. 1.0 *supra* at 3.



not be practical based on the fact that PREPA would be unable to meet its basic obligations as an electric utility.²⁴ Quintana further notes that currently PREPA's rates do not cover its costs, including operating expenses, capital improvements, debt service and legal obligations. Therefore, according to Quintana, current rates are not sufficient to provide service to its customers. The operation of PREPA under a deficit has led to degradation of its infrastructure and services, reducing reliability of the electric system, among other things.²⁵

Finally, pursuant to the requirement of Section 2.02(D) of Regulation No. 8720, PREPA has requested that the provisional rates come into effect thirty (30) days from the Commission's approval of such rates.²⁶

IV. COMMISSION DECISION

The Commission determines that PREPA has complied with the requirements of Regulation No. 8720, and has demonstrated and justified the need of implementing provisional rates. The Commission now needs to determine (1) the total amount of increased revenue to be paid through the provisional rates, (2) the allocation of that increased revenue among customer classes and customers, and (3) the effective date of the provisional rate increase.

On the issue of "revenue increase": PREPA has demonstrated a need for enhanced cash flow. As explained by Donahue and Quintana, PREPA is now, and has been since the forbearance agreement with part of the bondholders, operating on a cash basis and therefore not like a normal utility. PREPA is unable to access capital markets, is not paying either interest or principal to its participating bondholders, and is retaining those amounts, along with any income generated by current rates, for operating purposes. The Commission therefore approves the increase in the amount sought by PREPA—\$222,256,790.

On the issue of allocation: The Commission **DOES NOT APPROVE** PREPA's recommended allocation of the increase among customer classes. PREPA's proposed allocation relies on the "cost of service study" (COSS) filed with the Petition to support permanent rates. Such study makes many assumptions about the classification and allocation of costs. The complexity of these assumptions prevents the Commission, at this early stage of review, from confirming their suitability as a basis for permanent or provisional rates.

On 24 June 2016, PREPA filed supplemental testimony modifying its original proposal to account for the fact that public housing customers under Article 3.9(b) of Act 22-2016 do not pay a per-kWh charge on the first 600 to 1,000 kWh of monthly consumption, depending on the size of the housing unit. PREPA proposes to allocate the

²⁴ Ex. 10.0, *supra*, at 7.

²⁵ Ex. 1.0, *supra*, at 3.

²⁶ Petition, at 20.

responsibility for the revenues not collected from such customers to the remaining residential customers, thereby raising the percentage of total provisional rate revenue charged to residential customers. The Commission **DOES NOT ACCEPT** that proposal.

Instead of PREPA's proposed allocation, the Commission authorizes a uniform rate increase among all customer classes in an amount necessary to produce the \$222,256,790 in new revenue. Therefore, the Commission approves a uniform increase of 1.299 ¢/kWh, to be added to the existing per kilowatt hour (kWh) base rate for energy consumption for all customer classes. This approach to allocation is just and reasonable, because it addresses PREPA's immediate need for cash flow while not prejudging the proper allocation of revenues in the permanent rates. The provisional rate increase authorized herein shall not modify the rider that recovers the cost of fuel and purchased power.

Two clarifications to the foregoing requirement: For customers who, under Article 3.9(b) of Act 22-2016 and under PREPA's tariffs implementing said Article 3.9(b), pay a fixed charge for the applicable consumption-based block of electricity, as such blocks are established as of the date on which the Commission approves the provisional rates and as they may be adjusted from time to time as provided in Article 3.9(b)(4) of Act 22-2016, the provisional rate increase will apply only to consumption in excess of their applicable consumption-based block. The costs not recovered from public housing customers are allocated equally to all customers and are already included in the 1.299 ¢/kWh rate increase. Furthermore, stemming from the fact this is an addition to current rates —rather than a new charge— the provisional rate increase shall apply to net-metering customers only on their net consumption.

It is important to emphasize that the Commission's approval of provisional rates shall not be construed as an implicit approval of capital and/or extraordinary expenditures being reviewed by this Commission in the Integrated Resource Plan proceeding or in the general rate case. PREPA **is not authorized** to make capital expenditures on any project until express approval from the Commission is furnished. The provisional rate approved in this Order is temporary and has the intention of allocating revenue resources to PREPA in order to improve its current financial situation and allow its continued operation.

The Commission has determined that it needs additional information to determine the tracking mechanism PREPA shall implement through the effective term of the provisional rates, in order to perform the reconciliation process required by Act 57-2014 and Act 83. The Commission, at its discretion, may issue additional information requests in order to determine the most effective mechanism for PREPA to collect and track the information needed to perform the aforementioned reconciliation. Before the provisional rates come into effect, the Commission will issue an order in relation to the tracking and reconciliation method PREPA shall implement.

On the issue over the "effective date of the provisional rate": Pursuant to the discretion conferred by Section 6.25(d) of Act 57-2014 and Section 6A(e) of Act 83, the Commission approves PREPA's request to implement the provisional rate thirty (30) days after the notification date of this Order.

In light of the aforementioned, the Commission **GRANTS** PREPA's petition for provisional rates, **as modified by this Order**, which shall come into effect thirty (30) days after the notification date of this Order. Within five (5) days of the notification of this Order, PREPA shall publish in a general circulation newspaper, and on its website, a public announcement notifying the general public the Commission's determination regarding provisional rates. Such announcement shall also be included along with the first bill sent by PREPA to its customers after the date in which the Commission notifies its ruling regarding the establishment of provisional rates. The announcement shall include, but is not limited, to:

- (1) a detailed description of the Provisional rate authorized by the Commission, including the percentage change in relation to then current base rates;
- (2) the date in which the Provisional rate shall enter into effect; and
- (3) an explanation regarding the nature of the provisional rate and its effectiveness during the rate review process conducted by the Commission.²⁷

PREPA shall certify to the Commission compliance with the aforementioned and shall provide copy of such public notices no later than three (3) days from the date they are published.

If a party does not agree with this determination, the party adversely affected by this final Order may file a request for reconsideration before the Commission which shall state in detail the grounds in support of its application, and the remedy that, in his view, the Commission should have granted pursuant to Section 11.01 of Regulation 8543 and the applicable provisions of Act. 170 of August 12, 1988, as amended, known as the Uniform Administrative Procedures Act (LPAU, for its acronym in Spanish). The request to that effect must be filed within twenty (20) days from the date of filing of the notice of this Order by personal delivery to the Secretary of the Commission, temporarily located on the Board Telecommunications Regulatory at 500 Ave. Roberto H. Todd, San Juan PR 00907-3941.

The Commission, within fifteen (15) days of the filing of said request for reconsideration, shall consider such motion. If the motion is dismissed or no action is taken within fifteen (15) days, the period for requesting review will begin to run again from the notification of said dismissal or the completion of the fifteen (15) days, as appropriate. If a determination is made on the motion, the term to request review shall begin to run from the date on which a copy of the notification of the decision of the Commission finally resolving the motion for reconsideration is filed in the case. Such decision shall be issued and filed within ninety (90) days following the filing of the motion for reconsideration. If the Commission accepts the motion for reconsideration but fails to take any action with respect to the motion within ninety (90) days of it being filed, the Commission will lose jurisdiction over it and the term to request judicial review shall begin to count from the expiration of the term of ninety (90) days, unless the Commission, for just cause and within

²⁷ Section 2.02 Regulation No. 8720.

those ninety (90) days, extends the term to issue a decision for a period not to exceed thirty (30) days.

In the case an adversely affected party chooses not to follow the above administrative review procedure, said party may, within thirty (30) days from the date of filing of the notice of this Order, file for judicial review before the Court of Appeals of Puerto Rico. The foregoing, pursuant to Section 11.03 of Regulation 8543 and the applicable provisions of the LPAU. If the date of filing of the notice of this Order is different than the date of the deposit in the mail of said notice, the thirty (30) day term for judicial review shall be computed from the date of the deposit in the mail of the notice of the filing of this Order as evidence by the postmark. Any party filing for review of this Order shall notify the Commission and any other party notified by the Commission in this Order within the time allotted for review of this Order pursuant to applicable law and regulations. The filing, presentation and notification of the filing for judicial review shall comply with the applicable provisions of LPAU and the Regulation of the Court of Appeals of Puerto Rico, 2004 TSPR 121.

For the benefit of all the parties involved, the Commission issues this Order in both Spanish and English languages. Should any conflict between each version arise, the English version shall prevail.

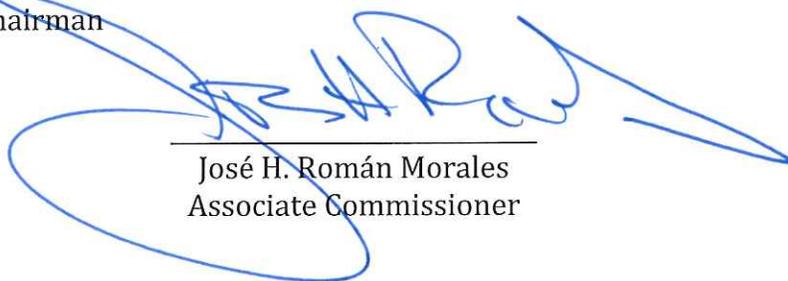
Be it notified and published.



Agustín E. Carbó Lugo
Chairman

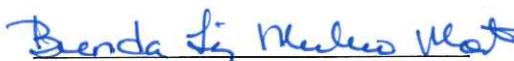


Ángel R. Rivera de la Cruz
Associate Commissioner



José H. Román Morales
Associate Commissioner

I certify that the Puerto Rico Energy Commission has so agreed on June 24, 2016. I also certify that on this date a copy of this Resolution and Order was notified via email to n-ayala@aepr.com, c-aquino@aepr.com, glenn.rippie@r3law.com & michael.guerra@r3law.com.



Brenda Liz Mulero Montes
Interim Clerk



CERTIFICATION

I Certify that the foregoing is a true and exact copy of the Resolution and Order issued by the Puerto Rico Energy Commission. I further certify that on June _____, 2016 I have proceeded with the filing of this Resolution and Order and I have sent a copy thereof to:

Puerto Rico Electric Power Authority
Attn.: Nérida Ayala Jiménez
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For the record, I sign this in San Juan, Puerto Rico, today, June _____, 2016.

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Rafael O. García Santiago
Clerk of the Puerto Rico
Telecommunications Regulatory Board