

June 23, 2016

VIA ELECTRONIC AND REGULAR MAIL:

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Ms. Nélide Ayala Jiménez
General Counsel
Puerto Rico Electric Power Authority (PREPA)
PO Box 363928
San Juan, PR 00936-3928

Re: *In re*: Review of Rates of the Puerto Rico Electric Power Authority, No. CEPR-AP-2015-0001; 2nd Requirement of Information

Dear Ms. Ayala,

Pursuant to the provisions in Article VIII of Regulation No. 8543, known as the Regulation on Adjudicative, Notice of Noncompliance, Rate Review and Investigation Proceedings (Regulation 8543), the staff of the Puerto Energy Commission (Commission Staff) is conducting discovery in the matter *In re*: Review of Rates of the Puerto Rico Electric Power Authority, No. CEPR-AP-2015-0001.

Through this letter, the Commission Staff issues a first round of requirements of information. With regard to this first round of requirements of information, PREPA shall submit, **on or before July 5th, 2016**, the information, data or documents, as appropriate, in digital format, required in Part II below. PREPA shall submit such information, data or documents in accordance with the following instructions:

I. Instructions

A. In General

1. Unless the context requires otherwise, all words used in the singular shall be deemed to also include the plural.
2. Responses to questions must be made in writing, separately and under oath. Questions should be answered by supplying any information which PREPA has knowledge of or information obtained by their representatives, employees, contractors, agents or representatives, or

as a result of any investigation conducted. Each response shall state the person responsible for that response.

3. When production of a document is required, the response should identify the document produced, the format or formats in which the document was produced, and the method and date it was delivered to the Commission Staff. The identification of the document shall include: the name or title of the document, the document date, and the name of its author.
4. If information, data or documents required for any requirement do not exist, the person to whom this request for information is directed shall so specify in his or her reply to that request.
5. Except where the context indicates otherwise, the term "any" includes "all," and vice versa.
6. PREPA shall have a continuing duty to update, correct or amend its answers and notify the Commission Staff of any additional information obtained after said request and which is the subject of this requirement of information.
7. For purposes of this requirement of information, the term "document" means any material, no matter the form, type, nature or description, whether electronic, handwritten or typed, printed, engraved, photographed or copied, and no matter by whom it was originated, prepared, produced, reproduced, published or disseminated. The term "document" includes all types of publications, reports, magazines, books, pamphlets, brochures, folders, records, and/or volume set of attached or unattached papers.
8. For purposes of this requirement of information, the term "information" includes data and documents.
9. Digital Format: All documents must be submitted in the Word or searchable PDF format. Analyses prepared using an electronic spreadsheet program such as Excel will be provided in native format with formulas and cross-references intact. Under no circumstances may a printed document, scanned and converted to an image in Personal Document Format (PDF), be presented if there is already a version in digital text. In view of this, the presentation of PDF images of documents that were originally produced in digital text will not be allowed. The presentation of PDF images will only be allowed for those documents that do not exist in a digital version, or for which PREPA does not have a digital version.

10. If PREPA finds it necessary to request an extension of time for the production of part of the required information, it shall do so in writing and submit its request to the Commission's Staff on or before *July 5th, 2016*. In its request, PREPA shall state the efforts undertaken thus far in order to produce the required information, and the reasons pursuant to which it will not be able to produce it within the original period, and which, according to PREPA, justify the granting of the requested extension, along with the specific date by which PREPA commits to provide a full response. However, on or before *July 5th, 2016*, PREPA shall produce all the required information that, up until that date, it has been diligently able to obtain, organize, and process in accordance with the instructions established in this letter.

B. Allegedly Confidential or Privileged Information and Documents

The Commission Staff recognizes that PREPA may assert that some of the documents responsive to these questions warrant confidential treatment. Section 1.15 of Regulation No. 8543, together with the provisions of Articles 1.4 and 6.15 of Act 57-2014, as amended, govern the information that may be unavailable for public access because it is privileged or confidential, as well as the general guidelines for the Commission to determine what information is privileged and confidential and the treatment to be given to protect such information.

Specifically, Section 1.15 of Regulation 8543 provides that when a person has the duty to submit to the Commission information that, in his or her view is privileged or confidential, that person shall (i) identify the information which he or she considers to be privileged or confidential, (ii) request the Commission to protect this information, and (iii) state in writing the arguments in support of his or her request for protection. Once the matter is submitted to the Commission, it shall proceed as provided in Article 6.15 of Act 57-2014 if the Commission determines that the information produced and identified deserves protection.

With this background, if any of the requirements of information require PREPA to submit information it understands is confidential or privileged, the following instructions shall be observed:

1. When submitting the information, PREPA shall (i) mark or identify the information as "confidential" or "privileged"; and "(ii) identify the reason why the document or information should be classified as "confidential" or "privileged".
2. No later than 10 days after submitting the information, PREPA shall submit a memorandum of law stating in writing the legal basis and sources to support its argument that the information or documents identified should be classified as "confidential" or "privileged". In its

memorandum, PREPA must connect each claim to a particular document or piece of information.¹ PREPA shall serve a copy of its memorandum of law to the intervenors currently participating in the proceeding.

3. Except for communications covered by attorney-client privilege, PREPA cannot fail to submit any information or document to the Commission on the grounds that it believes it is a confidential or privileged document or information. If PREPA claims that the information is attorney-client privileged, it must state the basis for this claim and affirmatively state that there is no other alternative way for PREPA to provide the information that would not be attorney-client privileged.
4. The Commission Staff will protect and maintain secure any and all information marked by PREPA as “confidential” or “privileged” unless the Commission rules otherwise.

C. Questions about the Requirements

If PREPA has any question about any of the requirements of information made in this letter, it shall state its question or need for clarification in writing and submit it by electronic mail to the Commission Staff. While PREPA and the Commission Staff may have verbal discussions about PREPA’s questions for efficiency purposes, all final questions and answers must be stated in writing. Verbal expressions and discussions about PREPA’s questions will have no evidentiary value or effect.

II. Requirements of Information

A. Questions for Witness Quintana

1. SGH-01-01: Ref. Quintana Direct, ll. 426-432 - At the cited portion of his testimony, Dr. Quintana states that a PREPA’s 2015 financial statements are not yet available due to a “change in the scope and breadth of the FY 2015 audit,” and a disagreement with PREPA’s auditor regarding the costs and fees related to that change in scope. Dr. Quintana cites PREPA Ex. 1.02 [an affidavit from the PREPA Chief Financial Officer (CFO)], for support. However, in PREPA Ex. 1.02 the CFO states that the change in scope was related to PREPA’s FY 2014 financials, not FY 2015. Please respond to the following questions:

¹ When handling “confidential” or “privileged” information, the Commission Staff will observe all the applicable rules from the *Normas Internas para el Manejo de Información Confidencial en la Comisión de Energía de Puerto Rico*. See, <http://energia.pr.gov/wp-content/uploads/2015/05/20150512141506478.pdf>

- a. Was the change of scope related to the Company's 2014 or 2015 financials?
 - b. If the change of scope was related to PREPA's 2014 financials, please explain in as much detail as possible what caused the change in scope, explain how it was accounted for and provide comparative 2014 financial statements before and after the change in scope.
 - c. If the change of scope was related to PREPA's 2015 financials, please explain in as much detail as possible what caused the change in scope, explain how it was accounted for and provide comparative 2015 financial statements before and after the change in scope, as soon as available.
 - d. The November 2014 FTI Capital Advisors Report indicates that PREPA has differences in its accounts receivable balances for financial reporting purposes and for operational reports used by its customer service personnel. Is this still the case and, if so, why?
2. CEPR-SGH-01-02: Ref. Quintana Direct, l. 599 - Dr. Quintana indicates that a Formula Rate is "called for" by the RSA. Please cite the portion of the RSA to which he refers, and explain if "called for" means "mandated" or "allowed."

B. Questions for Witness Donahue

1. CEPR-SGH-01-03: Ref. Donahue Direct, ll. 6-7 - Ms. Donahue testifies that she is the Chief Restructuring Officer of PREPA. Please describe the purpose of the \$625 Million of "Lender Bonds" described at pages 9 and 10, sub-paragraph "f." of the PREPARC Verified Petition for Restructuring Order.
2. CEPR-SGH-01-04: Ref. Donahue Direct, ll. 71-73 - Ms. Donahue indicates that, at July 1, 2016, PREPA has a \$1.3 Billion principal and interest payment due related to Revenue Bonds and Revolving Credit Lines. Is it correct that PREPA has reached an agreement with its Credit Lenders as part of its Securitization; and, if so, are those monies still due and payable on July 1, 2016? If not, please explain why Ms. Donahue elected to include the Revolving Credit obligations in her description of PREPA's July 2016 obligations.
3. CEPR-SGH-01-05: Ref. Donahue Direct, ll. 180-188 - Ms. Donahue indicates that by 2015, PREPA's revenues were approximately 8¢ to

12¢ per kWh lower than the Company's costs. Please provide the supporting analysis for those estimates, including all assumptions.

4. CEPR-SGH-01-06: Ref. Donahue Direct, l. 242 - Ms. Donahue indicates that PREPA needs to replenish its self-insurance fund. Is the replenishment of that fund planned for in the proposed Restructuring? If not, please explain why not.
5. CEPR-SGH-01-07: Ref. Donahue Direct, ll. 287-291 - At the cited portion of Ms. Donahue's testimony she discusses "noneconomic contingencies" that must be met under the Restructuring Support Agreement. Two of those items listed are 1) consent by holders of \$2 billion of the \$2.7 billion in bonds that are not currently parties to the RSA, and 2) the appointment of a new independent board of directors for PREPA. Please respond to the following questions:
 - a. What are the non-participating bondholders consenting to; the Restructuring?
 - b. What constitutes "consent" of the bondholders referenced, and how will that "consent" be determined and conveyed to PREPA?
 - c. Does the ratio of \$2 billion to \$2.7 billion (approximately 75%) have significance in the consent? Is it a required proportion?
 - d. Is it possible that some portion of those currently non-participating bondholders will elect to accept the new Securitized debt? If not, why not?
 - e. Please describe the progress, thus far, in selecting and installing the new PREPA board.
 - f. When is the new board expected to have its initial meeting?
6. CEPR-SGH-01-08: Ref. Donahue Direct, l. 398-399 - Ms. Donahue's testimony indicates that PREPA's rate case should be based on a formula rate model according to Schedule VI of the RSA. Is it Ms. Donahue's understanding that the Commission, in setting PREPA's rates must follow a formula rate model; and, if it does not, would that jeopardize the RSA? Please explain and provide any available supporting documentation.
7. CEPR-SGH-01-09: Ref. Donahue Direct, l. 396-399 - At the cited portion of her Testimony, Ms. Donahue indicates that Restructuring will not solve PREPA's "July 1" problems.

- a. Please explain how a 1.29¢ per kWh rate increase allowed on June 30, as requested by PREPA would solve PREPA's "July 1" problems, and provide supporting revenue and debt service calculations.
- b. Is it correct to understand that PREPA is currently expecting to finance its "July 1" problems with 2016 series bonds, the cost of which will be rolled into the Transition Charge that accompanies the Restructuring. If that is not the case, please explain why not.

C. Questions for Witness Miranda, Sales, Sosa ("M/S/S")

1. CEPR-SGH-01-010: Ref. M/S/S Direct, ll. 334-335 - What are PREPA's renewable energy portfolio requirements?
2. CEPR-SGH-01-011: Ref. M/S/S Direct, ll. 336-339
 - a. What is the expected annual amount, if any, of current and expected fuel cost savings from the conversion from oil to natural gas? Please provide supporting documentation.
 - b. What is the expected difference in CO₂ emissions from the conversion from oil to natural gas? Please provide supporting documentation.
3. CEPR-SGH-01-012: Ref. M/S/S Direct, l. 661 - To what extent is PREPA's "executive directorate" and "executive team" oversized. What positions should be eliminated and what would be the annual cost savings of eliminating those positions? Please provide supporting documentation.
4. CEPR-SGH-01-013: Ref. M/S/S Direct, Chart, p. 37
 - a. Please describe in as much detail as possible the \$109 Million "SPV Gross-up" included in the "Restructured PREPA/SPV Cost Structure 2017," identifying each component of that amount. Provide supporting documentation and analysis.
 - b. What portion of the \$709 Million of "Debt Service" represent PREPA debt? (as separate from debt to be owned by PREPARC or "the SPV")
5. CEPR-SGH-01-014: Ref. M/S/S Direct, ll. 783-788 - The witnesses indicate that in creating a sales forecast PREPA estimated the energy consumption and generation for FY 2015 by extrapolations of monthly data from 1993 through 2014.

- a. Given the volatility of those historical data, please explain that represents a reasonable methodology.
- b. Has any comparison been made, thus far, between the 2015 estimations that were used as the basis for forward sales forecast projections with the actual 2015 results? If not, why not?

D. Questions for Witness Zarumba and Granofsky (“Z/G”)

1. CEPR-SGH-01-015: Ref. Z/G Direct, ll. 674-675 - At the cited portion of the witnesses’ testimony a process to update tariffs is discussed but begins with #5. Have four steps been eliminated or is the list mis-numbered?

E. Questions for Witness Pampush, Porter and Stathos (“P/P/S”)

1. CEPR-SGH-01-016: Ref. P/P/S Direct, ll. 361-373 - The witnesses indicate that the debt service for PREPA’s legacy (non-securitized) debt is approximately \$3.14 Million, the debt service for the SPV (PREPARC) is approximately \$394 Million, and that PREPA’s bond covenants require a DSCR of 1.20. Please respond to the following questions:
 - a. Are the debt service amounts cited for the 2017 rate year (7/1/2016 through 6/30/2017)? If not, please explain why not and identify the period for which the debt service amounts are pertinent.
 - b. Please list, with reference to PREPA’s Sch. D-2 electronic worksheet the individual debt issues used in determining PREPA’s legacy debt service. If the witness are unable to answer this question, or the interest and principal for 2017 for the debt issued identified do not sum to approximately \$314 Million, please explain precisely how the \$314 Million debt service was estimated.
 - c. Please list, with reference to PREPA’s Sch. D-2 electronic worksheet, the individual debt issues used in determining PREPA’s Securitized debt service. If the witness are unable to answer this question, or the interest and principal for 2017 for the debt issued identified do not sum to approximately \$394 Million, please explain precisely how the \$394 Million debt service was estimated.

- d. What is the total amount of PREPA legacy debt for which the \$314 debt service Million is applicable, based on the amount outstanding?
 - e. What is the total amount of SPV (PREPARC) debt for which the \$394 debt service Million is applicable, based on the amount outstanding?
 - f. Does the DSCR of 1.20 required by the bond covenants apply to the PREPA legacy debt only? If not, please explain why not.
 - g. In preparing their revenue requirement did the witnesses apply a DSCR to both PREPA debt and SPV (PREPARC) debt? If so, please explain why, and if not, please explain why not.
 - h. What was the DSCR used in determining PREPA's revenue requirement?
2. CEPR-SGH-01-017: Ref. P/P/S Direct, ll. 649-651 At the cited portion of their testimony, the witnesses indicate that the PREPA legacy debt service is composed of equal parts non-participating PREPA bonds and a 5-year amortization of fuel and GDB lines of credit.
 - a. Are the witnesses aware of the \$625 Million of "Lender Bonds" that are to be issued as part of the Restructuring (see pages 9 and 10, sub-paragraph "f." of the PREPARC Verified Petition for Restructuring Order)? If not, please so state. If so, please provide the witnesses understanding of the purpose of those PREPARC bonds and how they are different from the "fuel and GDB" lines of credit discussed at the cited portion of their testimony.
 - b. If the fuel and GDP short-term debt amortization obligations of PREPA are currently accounted for in the Restructuring proceeding and will be included in the Transition Charge, please explain why those obligations should also be included in the rate proceeding? If they should not be included in the PREPA rate case, please so state.
 3. CEPR-SGH-01-018: Ref. P/P/S Direct, ll. 658-660. - The witnesses state that the debt service costs discussed in the Cash and Modified Cash ratemaking bases are "subsumed" in the rate of return approach. Please show that the total debt costs that result from the rate of return approach equal approximately \$314 Million for PREPA in 2017.
 4. CEPR-SGH-01-019: Ref. P/P/S Direct, l. 753, PREPA Ex. 5.08

- a. Please provide, in Excel format, the RRA data used to create the graph in Ex. 5.08, including the name of each company, the date of the order, equity return, equity ratio, and overall return.
 - b. Are the debt returns reported in the RRA publication embedded cost rates (based on the accounting value of the debt on the books of the utility), or are they marginal debt costs (based on current market values and interest rates)? Please explain.
5. CEPR-SGH-01-020: Ref. P/P/S Direct, ll. 769-770
 - a. Please explain why it is reasonable to apply a marginal cost of debt capital to a book value rate base.
 - b. What is the current embedded cost rate of PREPA debt? Please provide all supporting workpapers.
6. CEPR-SGH-01-021: Ref. P/P/S Direct, ll. 852-854 - The witnesses testify that “significant investment is underway” regarding converting generation from fuel oil to natural gas. Please identify the projects referenced. Has this capital investment been undertaken prior to the approval of an IRP by the Commission? If so, what is the current level of investment and what is anticipated in the remainder of 2016 and 2017?
7. CEPR-SGH-01-022: Ref. P/P/S Direct, l. 947, Ex. 5.14
 - a. Are the DSCR values shown on Ex. 5.14 for coverage of PREPA and SPV (PREPARC) debt? If not, please indicate the debt base on which those coverage ratios are calculated.
 - b. Please provide, in spreadsheet format, the data used to create the graph in Ex. 5.14.
 - c. Please explain why the DSCR coverages shown for 2017 are substantially different from those discussed by the witnesses at lines 789-803, and provide the supporting data for each DSCR estimate.
8. CEPR-SGH-01-023: Ref. P/P/S Direct, ll. 959-960 - Provide support for the witnesses’ statement that, for rating agencies, balance sheet common equity levels are a key indicator of financial health for municipal utilities.

9. CEPR-SGH-01-024: Ref. P/P/S Direct, p. 49 - Please provide complete copies of the credit rating reports cited in the footnotes. The web addresses cited did not work.
10. CEPR-SGH-01-025: Ref. P/P/S Direct, p. 50, footnote 17 - Please provide a complete copy in electronic form at the Fitch Public Power study cited.
11. CEPR-SGH-01-026: Ref. P/P/S Direct, l. 1261 - Please explain how the classification tree approach is “relatively robust to outliers,” as measured by what criterion?
12. CEPR-SGH-01-027: Ref. P/P/S Direct, p. 63
 - a. Please explain why truncating the sample a) is a reasonable response to skewness and b) why the results of analyzing the smaller sample are expected to provide a reliable indication of the results that would be obtained with the original sample.
 - b. Is the statistical significance of the results reduced? If so, to what extent in this case?
13. CEPR-SGH-01-028: Ref. P/P/S Direct, l. 1444 - Please provide a rating agency definition of “Full Obligation Coverage.”

F. Question for Witness Kaufman

1. CEPR-SGH-01-029: Ref. Kaufman Direct, Exhibit 6.01 - Please provide a complete copy of Consulting Project No. 5 listed in Dr. Kaufman’s vitae, a cost benchmarking study for PREPA in 2015.
2. CEPR-SGH-01-030: Ref. Kaufman Direct, ll. 345-347] - Was the data for the electric utility in Hawaii for Hawaiian Electric Industries or Hawaiian Electric Company?

G. Questions for Witness Hemphill

1. CEPR-SGH-01-031: Ref. Hemphill Direct, Ex. 7.01 - Please provide a complete copy of Dr. Hemphill’s 2014 *Electricity Journal* article cited in his vitae.
2. CEPR-SGH-01-032: Ref. Hemphill Direct, ll. 124-125 - Dr. Hemphill testifies that there are no differences between traditional regulation and a formula rate mechanism with regard to the components used to calculate the revenue requirement. Please list the differences that

do exist between traditional rate base/rate of return regulation and a formula rate mechanism.

3. CEPR-SGH-01-033: Ref. Hemphill Direct, ll. 271-272 - Please explain how being “government-owned” prevents access to the capital markets.
4. CEPR-SGH-01-034: Ref. Hemphill Direct, ll. 432-436 - Please explain what is meant by a “DSCR adjusted for total cost of capital,” and provide a cite to a portion of PREPA’s filing in this proceeding where that concept is discussed.
5. CEPR-SGH-01-035: Ref. Hemphill Direct, ll. 450-453 - Please provide the support on which Dr. Kaufman relies to show that traditional ratemaking “more often than not” causes overstated rates.

H. General Questions

1. CEPR-SGH-01-036: Please provide a calculation showing the embedded cost rate of each of the PREPA legacy debt issues that will remain on the PREPA balance sheet after the Restructuring. Please provide supporting documentation.
2. CEPR-SGH-01-037: Ref. Sch. D-2 Worksheet
 - a. Are the bonds listed on tab D-2A all of PREPA’s bonds outstanding in May 2016, i.e., including those that are to be Restructured? If not, please explain why the combined debt service for 2017 shown on that tab is \$637 Million rather than \$314 Million.
 - b. Please identify each of the bonds that is expected to remain on PREPA’s books after the Restructuring.
 - c. Does PREPA have any bond or other debt obligations that are not shown on tab D-2A of Sch. D-2 Worksheet? If so, please provide a listing of those obligations with the same data that is included in D-2A of Sch. D-2 Worksheet, and explain why they were omitted.
 - d. Please provide the coupon rate and issuance costs associated with each bond issue listed on tab D-2A of Sch. D-2 Worksheet.
 - e. Please explain why the interest for 2017 is presented as net of “estimated subsidies,” and explain what those subsidies are.

3. CEPR-SGH-01-038: Ref. Regulation 8720, Section 2.13(A), Schedule K-1-PREPA Affiliates - Please respond to the following questions regarding PREPA Holdings and its affiliates:
 - a. Please provide the income statements, cash flow statements and balance sheets for the most recent two years for each of the affiliates within PREPA Holdings: PREPA Networks, Consolidated Telecom of Puerto Rico, and InterAmerican Energy Sources. If the Company is unable to comply with this request, please explain why.
 - b. Why do these affiliates (PREPA Networks, Consolidated Telecom of Puerto Rico, InterAmerican Energy Sources) exist?
 - c. Do these affiliates (PREPA Networks, Consolidated Telecom of Puerto Rico, InterAmerican Energy Sources) operate within PREPA and contribute to PREPA's bottom line, or does PREPA contract with the affiliates for their services, and, therefore, do their charges to PREPA appear as expenses on PREPA's income statement? Please explain the arrangement for each of the three affiliates.
 - d. If PREPA Holdings three affiliates are operated as contractors to the utility (as opposed to cost centers within the utility), please indicate where the charges related to those operations are found in PREPA's rate filing.
 - e. Do these affiliates hire their own employees or do they utilize the services of PREPA employees; and, if the latter is the case, please explain how the cost of those employees is allocated between PREPA and the affiliates.
 - f. How many employees does each of the three affiliates have?
 - g. Please explain why PREPA Holdings has two separate subsidiaries (PREPA Networks, and Consolidated Telecom of Puerto Rico) that do the same type of work and have the same board members.
 - h. Please describe the operations outside the Commonwealth of Puerto Rico of each affiliate (PREPA Networks, and Consolidated Telecom of Puerto Rico).
 - i. Please explain whether or not a conflict of interest exists between PREPA and its sales of traditional utility-sourced power and InterAmerican Energy Sources, which "develops, finances,

constructs and operates” renewable power projects? If not, please explain why not.

- j. Please provide recent examples to explain how and to what extent InterAmerican Energy “finances” and “constructs” renewable and non-renewable power projects.
- k. Has InterAmerican Energy Sources “financed” or “constructed” any projects during the period of PREPA’s forbearance agreement with creditors? If so, please describe those projects.
- l. Was the operation of PREPA Holdings and its affiliates restricted in any way or addressed by the forbearance agreement with PREPA’s creditors? If so, how?

Responses to the requirements of information shall be submitted electronically by electronic mail to the following addresses: afigueroa@energia.pr.gov, tnegron@energia.pr.gov, and gbonet@energia.pr.gov. If responses are too voluminous to be sent by electronic mail, the responses shall be saved in a USB device and sent by mail with return receipt to: Cecilia Sánchez, 268 Muñoz Rivera Ave., World Plaza Suite 703, San Juan, PR 00918.

Cordially,

/s/ Alejandro J. Figueroa Ramírez, Esq.

/s/ Tania M. Negrón Vélez, Esq.