

COMMONWEALTH OF PUERTO RICO
PUERTO RICO ENERGY COMMISSION



IN RE: PUERTO RICO ELECTRIC POWER
AUTHORITY RATE REVIEW

CASE NO.: CEPR-AP-2015-0001

SUBJECT: Motions for Reconsideration filed
by ICSE-PR, ICPO and PREPA.

RESOLUTION

This Resolution addresses the motions for reconsideration of the Puerto Rico Energy Commission's ("Commission") November 3, 2016 Resolution ("November 3 Resolution") filed by the *Instituto de Competitividad y Sostenibilidad Económica de Puerto Rico* ("ICSE-PR", by its Spanish acronym), the Independent Consumer Protection Office ("ICPO") and the Puerto Rico Electric Power Authority ("PREPA") on November 14, 2016, November 16, 2016 and November 21, 2016, respectively.

A. Introduction and Background

The November 3 Resolution identified certain cost allocation and rate design issues of which the Commission would defer consideration until a proceeding that will begin shortly after the conclusion of the instant proceeding. In such occasion, the Commission determined that the lack of precision in some of the information provided by PREPA, coupled with certain discrepancies found in PREPA's responses to discovery questions, prevented the Commission from reaching an informed and responsible determination with regards to specific areas related to cost allocation and rate design included in PREPA's Petition for Rate Review ("Petition").

In essence, ICSE-PR and ICPO argue that the Commission's determination regarding the insufficiency of the information provided by PREPA in relation to cost allocation and rate design requires the Commission to reject PREPA's Petition. ICPO further argues that, in lieu of rejecting PREPA's Petition, the Commission should not defer any determination related to cost allocation and rate design, regardless of the quality of the information available to support such determinations. Neither of the alternatives suggested by ICSE-PR and ICPO provides a satisfactory result.

On the other hand, in its Motion, PREPA concedes that the information provided in support of its cost allocations and rate design proposal is insufficient and does not allow for the development of an "optimal rate design."¹ Nonetheless, PREPA asks the Commission to reconsider its November 3 Resolution given that adopting PREPA's proposed rate design is a better alternative than rejecting it. The Commission disagrees with PREPA's assertion.

¹ See, PREPA's Informative Motion Requesting Reconsideration and Deferral of Order, p. 2, at 4.

B. The November 3 Resolution, Cost Allocation and Rate Design

Contrary to the arguments of ICPO, the November 3 Resolution did not defer a determination by the Commission regarding the reasonableness of the costs identified by PREPA in its Petition. This responsibility, which is part of the evaluation of PREPA's proposed revenue requirement, is at the center of the determinations that the Commission will make in the instant proceeding. In issuing its final resolution and order, the Commission will determine what is PREPA's reasonable and appropriate revenue requirement for fiscal year 2017.

What the Commission intends to address and achieve, in a proceeding to begin shortly after the final resolution and order in the instant proceeding, is: (1) a comprehensive, in-depth and methodical analysis of PREPA's cost of service study ("COSS") and (2) the allocation of revenue responsibility among customer classes in a manner that more appropriately reflects the costs of providing service to each customer category. To achieve these results, the Commission must have access to reliable, up-to-date information on the costs PREPA incurs to serve each customer class and each class's load and consumption patterns. Such detailed information is currently unavailable in the necessary form, accuracy and clarity.

The allocation of cost responsibility and revenue responsibility among customer classes is separate and independent from the determination of an appropriate revenue requirement. To establish just and reasonable rates, the Commission must first determine what is PREPA's overall revenue requirement (the total number of dollars PREPA must earn in a year in order to meet all of its operational and financial obligations). Once PREPA's revenue requirement has been determined, the Commission must allocate responsibility for collection of PREPA's revenue requirement among PREPA's customer categories (this process is known as revenue allocation). Revenue allocation is achieved by first determining the amount of PREPA's costs which are directly or indirectly caused by each specific customer class, and assigning responsibility for payment of those costs to such customer classes, taking into account various considerations such as gradualism and equity, among others. Then the Commission must determine the appropriate rate design (consisting of, potentially, customer charges, demand charges, consumption charges and riders and adjustment clauses) that will determine each individual customer's monthly bill.

While the aforementioned is an oversimplification, all four components (revenue requirement, cost allocation, revenue allocation and rate design) form the backbone of ratemaking procedure. However, while a traditional rate case may seek to achieve a determination on all four areas in the same proceeding, it is not necessary to do so; regulatory agencies can instead determine an appropriate requirement, then allocate revenue responsibility and design rates without having an up-to-date cost of service study. Such a proceeding can produce just and reasonable rates. The reality of cost-based ratemaking is that at any point in time, rates will not perfectly reflect costs.

The instant proceeding is not a traditional rate case. Among the challenges the Commission and intervenors must face is the fact that such detailed analysis has not been undertaken in recent years. The lack of reliable information regarding past outcomes and operations requires a much more labor-intensive and time-consuming analysis than is possible within the one hundred eighty (180) days the Legislature has granted the Commission to issue a final resolution in this case.² This is an inescapable fact. Given these challenges, the Commission has determined that it is unrealistic, and would be irresponsible, to seek to achieve an in-depth reform of PREPA's cost allocation and rate design proposal within the limited timeframe provided by Act 57-2014.³ Effective and meaningful reform requires time and effort, and the ability to overcome particular interest to ensure the common good. PREPA's transformation into an efficient and effective utility requires decisions which are based on solid facts.

Furthermore, the November 3 Resolution did not defer all cost allocation, revenue allocation and rate design issues to a later proceeding. Rather, it deferred only those specific issues within cost allocation, revenue allocation and rate design for which the lack of reliable information prevents the Commission from issuing an informed and duly-grounded decision. Moreover, given the questionable quality of the information that is available, any determination that treats such information as reliable would result in rates which deviate from a just and reasonable standard. While the Commission finds that its practical ability to determine cost allocation and revenue allocation is limited, the Commission will make those determinations for which there is sufficient and reliable evidence and which result in just and reasonable rates. The Commission expects all parties to understand these practical limitations and assist in producing a decision by January 11, 2017 that improves on the *status quo* and points PREPA in a positive direction.

With regards to PREPA's arguments, in addition to its determination regarding revenue requirement, the Commission will make several determinations regarding cost allocation, revenue allocation and rate design –to the extent those decisions can be supported by reliable evidence and to the extent those decisions will result in an improvement on the *status quo*. The Commission views this first rate proceeding as one step, and not the final step, in establishing rates that best serve electric power customers. The November 3 Resolution, therefore, was intended to signal to parties the infeasibility of making complete, comprehensive decisions on all aspects of cost allocation, revenue allocation and rate design, given the shortness of time and the inadequacy of the data. How the Commission ultimately draws the line between what it decides fully in this proceeding and what it decides partially or temporarily, will be a subject of discussion during the Technical Hearing. Finally, the Commission will determine, within this proceeding, the proper treatment of fuel costs, in terms of the relationship between base rate and adjustment clause.

² Ordinarily, a traditional rate case in which all four components of a rate review are analyzed and the utility seeking a rate review has a rich history of regulatory oversight takes anywhere between (12) to eighteen (18) months to conclude.

³ The Puerto Rico Energy Transformation and RELIEF Act, as amended.

C. Alternatives to the November 3 Resolution

ICSE-PR and ICPO argue that, in light of the insufficiencies identified in the November 3 Resolution, the Commission should reject PREPA's Petition. The consequences of such an action are far-reaching and have a significant, negative impact on consumers and on Puerto Rico's energy future.

Concluding the instant proceeding without evaluating PREPA's revenue requirement delays the progress necessary to a meaningful reform of PREPA's operations, and will create uncertainty for consumers, employees and investors. Puerto Rico needs a utility that is financially sound, fiscally responsible, operationally efficient and responsive to the needs of all its customers—residential, commercial and industrial; large, medium and small. Terminating this proceeding prematurely would leave Puerto Rico in the past rather than progressing toward the future. Act 57-2014 requires the Commission to approve a revenue requirement that is sufficient to cover PREPA's reasonable operational and financial obligations, along with rates that are just and reasonable and not unduly preferential. The information available in this proceeding is sufficient for the Commission to achieve those objectives. As previously stated, the absence of a reliable cost of service study does not prevent the Commission from determining the appropriate level of PREPA's revenue requirement.


Granting ICSE-PR and ICPO's requests would create uncertainty among PREPA's bondholders, employees, managers and executives; among the contractors that sell products and services to PREPA; and among the customers who need to see progress in the modernizing of PREPA's infrastructure, including the infrastructure necessary to ensure the integration of renewable energy and increase generation efficiency. Furthermore, failure to align PREPA's outdated rates to current costs would continue to exacerbate PREPA's liquidity problems, which may force PREPA's bondholders and creditors to take drastic actions to ensure payment of PREPA's debts.

In light of the aforementioned, the Commission **DENIES** the motions for reconsideration filed by PREPA, ICSE-PR and ICPO.

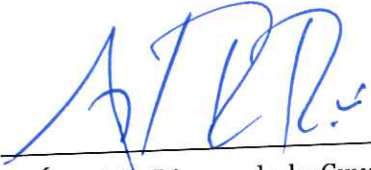
For the benefit of all parties involved, the Commission issues this Resolution in both Spanish and English languages. Should any conflict between each version arise, the English version shall prevail.

Be it notified and published.




Agustín F. Carbó Lugo

Chairman


Ángel R. Rivera de la Cruz
Associate Commissioner


José H. Román Morales
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CERTIFICATION

I hereby certify that the majority of the members of the Puerto Rico Energy Commission has so agreed on November 23, 2016 and on this date a copy of this Resolution was notified by electronic mail to the following: n-ayala@aeep.com, c-aquino@aeep.com, glenn.rippie@r3law.com, michael.guerra@r3law.com, john.ratnaswamy@r3Law.com, codiot@opic.pr.gov, jperez@oipc.pr.gov, mmuntanerlaw@gmail.com, jfeliciano@constructorespr.net, abogados@fuerteslaw.com, jose.maeso@aae.pr.gov, edwin.quinones@aae.pr.gov, nydinmarie.watlington@cemex.com, aconer.pr@gmail.com, epenergypr@gmail.com, jorgehernandez@escopr.net, ecandelaria@camarapr.net, pga@caribe.net, manuelgabrielfernandez@gmail.com, agraitfe@agraitlawpr.com, maribel.cruz@acueductospr.com, mgrpcorp@gmail.com, eirizarry@ccdlawpr.com, attystgo@yahoo.com and pnieves@vnblegal.com. I also certify that today, November 23, 2016, I have proceeded with the filing of the Resolution issued by the Puerto Rico Energy Commission and I have sent a true and exact copy to the following:

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For the record, I sign this in San Juan, Puerto Rico, today, November 23, 2016.

A handwritten signature in blue ink, which appears to read 'M. Cintrón', written over a horizontal line.

María del Mar Cintrón Alvarado
Clerk