COMMONWEALTH OF PUERTO RICO
PUERTO RICO ENERGY BUREAU

IN RE: PUERTO RICO ELECTRIC POWER AUTHORITY RATE REVIEW	**CASE NO.:** NEPR-AP-2023-0003 **SUBJECT:** Responses of PREPA Bondholders to Consultant Questions

RESPONSES OF PREPA BONDHOLDERS TO CONSULTANT QUESTIONS

National Public Finance Guarantee Corporation ("National"), GoldenTree Asset Management LP ("GoldenTree"), Syncora Guarantee, Inc. ("Syncora"), Assured Guaranty Inc. ("Assured"), and the PREPA Ad Hoc Group[1] (collectively, the "Bondholders"), by and through the undersigned counsel, hereby submit these responses to certain questions from the Energy Bureau's consultants in recent formal and informal orders in the above-captioned proceeding,[2] and in a January 10, 2025 Technical Conference (the "Jan. 10 Conference").[3]

The undersigned Bondholders hold or insure over 60 percent of outstanding principal amount of PREPA's bonds, which represent billions of dollars that PREPA borrowed over the years. The Bondholders have a perfected and unavoidable lien on all of PREPA's past, present,

[1] The members of the PREPA Ad Hoc Group are listed in the *Fourth Verified Statement of the PREPA Ad Hoc Group pursuant to Bankruptcy Rule 2019*, ECF No. 5279, filed in *In re Fin. Oversight & Mgmt. Bd.*, Case No. 17-BK-04780-LTS (D.P.R. July 8, 2024).

[2] *See Resolution and Order re: Requests of Information and Scheduling of Technical Conference for January 10, 2025*, Case No. NEPR-AP-2023-0003 (Dec. 20, 2024) ("Dec. 20 Order"); *Technical Conference of January 10, 2025: Consultant's Agenda and Explanation*, Case No. NEPR-AP-2023-0003 (Jan. 3, 2025) (the "Jan. 3 Questions") (the date listed on the Energy Bureau's website is January 13, 2025, however the Bondholders understand based on discussion at the Jan. 10 Conference that this document was distributed to PREPA, LUMA, and Genera on January 3, 2025); *Consultants' Request of Parties Arising from Technical Conference of January 10, 2025*, Case No. NEPR-AP-2023-0003 (Jan. 10, 2025) (the "Jan. 10 Questions") (as of the date of filing, this document had not yet been posted to the Energy Bureau's website; it was received upon request following the Jan. 10. Conference).

[3] The Bondholders are submitting these responses as invited by the Energy Bureau's consultants during this "informal" phase of the Rate Review. Based on a January 15, 2025 e-mail from Scott Hempling, the Bondholders understand that no parties have formally intervened, and intervention is not necessary at this time. The Bondholders reserve all rights to intervene at the appropriate time.

and future Net Revenues. *See generally In re Fin. Oversight & Mgmt. Bd.*, 121 F.4th 280 (1st Cir. 2024). PREPA's bondholders are the largest creditor group in its ongoing Title III case.

In the Jan. 3 Questions, the Jan. 10 Questions, and at the Jan. 10 Conference, the Energy Bureau's consultants raised questions related to the amount of PREPA's bond debt in connection with establishing PREPA's overall "revenue requirement." The revenue requirement is a buildup of "all costs and all revenues, regardless of source or payee."[4] The revenue requirement will ultimately be used in setting a new base rate—the first such adjustment since 2017—and it is therefore critical for the Energy Bureau and its consultants to consider accurate information and applicable law.

The Bondholders are deeply concerned about two possibilities that have been suggested by the Energy Bureau's consultants and/or the operators. ***First***, it has been suggested that PREPA's revenue requirement use one of the following amounts to reflect its multibillion-dollar bond debt obligations: (i) *zero dollars*; (ii) the Financial Oversight and Management Board's ("FOMB") last publicly available settlement offer from attempts to mediate its ongoing litigation with the Bondholders; (iii) the FOMB's proposed treatment of bondholders from its contested and now-defunct 2024 plan of adjustment; or (iv) some other number, *e.g.*, "halfway between the FOMB's position and the bondholders' claim."[5] But as the Energy Bureau recently stated, the revenue requirement should include "all costs and revenues," including the "debt that is subject to the Title III process."[6] And as the United States Court of Appeals for the First Circuit has conclusively determined in the Title III case, the minimum amount of the debt subject to the Title III process is

[4] Dec. 20 Order at p.3.

[5] Jan. 10 Questions at p.2; Jan. 10 Conference, available online at https://www.youtube.com/watch?v=s2AHsASbBB8 (last visited Jan. 17, 2025), at 1:00:38 to 1:04:16.

[6] Dec. 20 Order at p.3.

"the principal plus matured interest of the bonds, or roughly $8.5 billion."[7] The First Circuit has also held that PREPA's bondholders are "secured by PREPA's Net Revenues."[8] As a result, PREPA's bondholders are also entitled to post-petition interest if the value of their collateral exceeds the nominal amount of their claim.[9]

It would be inappropriate for the Energy Bureau to *sua sponte* discount PREPA's bond debt. The amount of the debt is readily, mathematically determinable.[10] Whether that amount might later be reduced—through a settlement or otherwise—is unknown at this time, and the amount is not subject to reduction except, if at all, through the Title III process. The Energy Bureau should use the full debt amount in establishing the revenue requirement; any reduction that might someday become necessary as a result of the Title III process can be made at the appropriate time following the Title III case. Until then, it remains a valid debt, as established by the First Circuit.

Second, it has been suggested that multiple budgets may be considered in this case: A so-called optimal budget reflecting PREPA's costs, and one or more so-called alternative budgets reflecting reductions to the optimal budget of as much as *75 percent.*[11] The only stated justifications for such reductions are that the optimal budget may "produce base rates higher than what the citizens are willing to pay," and that consideration of the alternative budgets may "help the Bureau decide, and explain to the public, the actual tradeoffs between rate levels and service

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[7] *In re Fin. Oversight & Mgmt. Bd.*, 121 F.4th at 312.

[8] *Id.* at 290.

[9] 11 U.S.C. § 506(b).

[10] *See id.* at 310 ("We conclude that the proper amount of the Bondholders' claim is the face value (i.e., principal plus matured interest) of the Revenue Bonds."); *see also* 11 U.S.C. § 101(5) (defining "claim" to mean "right to payment"); *id.* § 101(12) (defining "debt" to mean "liability on a claim").

[11] Jan. 3 Questions at pp.2-3; Jan. 10 Questions at pp.1-2; Jan. 10 Conference at 1:40:28 to 1:42:35.

quality."[12] The Bondholders respectfully submit that reducing PREPA's ability to recoup costs in order to avoid rate increases would be inappropriate. Indeed, a core reason for the Energy Bureau's creation was to address such suboptimal behavior by PREPA.[13] PREPA simply must charge customers what is necessary to cover its expenses. If certain customers cannot afford the resulting rates, then that issue should be resolved through reallocation of costs to other customers via rate design and/or through Commonwealth subsidies. But if the Energy Bureau does consider such reductions (it should not), that will make it all the more important to start from the full amount of the bond debt. Otherwise, the Bureau would be imposing a double haircut.

The Bondholders appreciate the time and attention that the Energy Bureau and its consultants have dedicated, and will dedicate, to this Rate Review, as well as the opportunity to participate as the case proceeds informally.

BACKGROUND

Puerto Rico passed the Puerto Rico Electric Power Authority Act in 1941, which permits PREPA to raise money by issuing revenue bonds.[14] In 1974, PREPA executed the Trust Agreement, with First National City Bank as Trustee, under which PREPA issued revenue bonds to raise money to finance its system.[15] PREPA promised to repay its bondholders in accordance with the Trust Agreement,[16] but PREPA defaulted on its payment obligations in 2017.[17] Each of

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[12] Jan. 3 Questions at pp.2-3.

[13] *See* Act 57-2014, Statement of Motives (creating the Energy Bureau's predecessor in part because "PREPA has become a monopoly that regulates itself [and] sets its own rates without actual oversight").

[14] *See* P.R. Laws Ann. tit. 22, § 206(e)(1); *see also id.* § 196(o).

[15] *In re Fin. Oversight & Mgmt. Bd.*, 121 F.4th at 290.

[16] *Id.*

[17] *Id.* at 292.

the undersigned Bondholders holds and/or insures PREPA bonds issued pursuant to the Trust Agreement, and these Bondholders collectively hold or insure over 60 percent of the outstanding principal amount of the PREPA bonds.[18]

A. PREPA and LUMA Have Persisted in Using an Outdated Base Rate

PREPA's base rate was last adjusted in January 2017, *eight years* ago.[19] During that time, PREPA has been impacted by, among other things, Hurricane Maria, the COVID-19 pandemic, a cluster of earthquakes, rapid inflation, and Hurricane Fiona. PREPA's mismanagement before and during that period has been well-documented. Notwithstanding these events, PREPA's base rate—the part of its overall rate meant to cover costs other than fuel and purchased power—has remained unchanged.

This is not how things were supposed to work. PREPA's base rate was intended to be reviewed and adjusted as needed every three years,[20] or more frequently if necessary.[21] Rate reviews should have included the establishment of "a new revenue requirement, a new cost of service, a new revenue allocation and a new rate design."[22] That is meant to ensure PREPA, like other utilities, collects an amount of revenue that aligns with its costs—as determined from the

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[18] *See Joint Informative Motion of GoldenTree Asset Management LP, Syncora Guarantee, Inc., Assured Guaranty Inc., National Public Finance Guarantee Corporation, and the PREPA Ad Hoc Group regarding Extension of Term of Cooperation Agreement*, Case No. 17-04780-LTS, ECF No. 5316, at p.2 (D.P.R. Aug. 19, 2024).

[19] *See Final Resolution and Order*, Case No. CEPR-AP-2015-0001 (Jan. 10, 2017) (the "2017 Rate Order"). The data underlying that rate was older still; the case began in May 2015. Prior to that case, PREPA's last rate adjustment was in 1989.

[20] 2017 Rate Order at pp.7, 149.

[21] *See* Act 57-2014, § 6.25(b) (allowing a rate review to be initiated as needed based on best interests).

[22] 2017 Rate Order at p.149.

ground up in a deliberate, data-driven process. Those costs include payment of PREPA's bond debt, as required by the Trust Agreement.[23]

But PREPA did not initiate this process. To the contrary, PREPA actively resisted or quickly abandoned any efforts to adjust the base rate. For example, in case CEPR-AP-2018-0002 the Energy Bureau stated, "the 2017 hurricanes have drastically affected PREPA's costs, revenues and expectations of future sales, making it unlikely that the rates in effect today satisfy the statutory 'just and reasonable' standard. The [Energy Bureau] therefore initiates this proceeding to set new rates."[24] Notably, the Energy Bureau also recognized the need to address debt service, which had been left out of the 2017 Rate Order, as discussed further below.[25] Rather than take this opportunity to adjust rates, PREPA opposed the Energy Bureau's order initiating a rate review, calling it "inconsistent with Puerto Rico and federal law," and attempted to stall the case at every turn.[26] PREPA moved for extension after extension of deadlines to submit required information, until the rate case was finally derailed by December 2018.[27] The rate was never adjusted, and nothing further was ever filed in that case.

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[23] *See, e.g., In re Fin. Oversight & Mgmt. Bd.*, Case No. 19-00391-LTS, Doc. No. 118, *Joint Informative Motion Submitting Conformed Trust Agreement*, at Ex. A pp.63-64 (D.P.R. Jan. 10, 2023) (PREPA covenanting to "at all times fix, charge and collect reasonable rates and charges" sufficient to service the debt, with a 120% debt service coverage ratio, and "from time to time, and as often as it shall appear necessary, [] adjust such rates and charges so that the Revenues will at all times be sufficient"). When the Trust Agreement was executed, PREPA had the ability to set its own rates.

[24] *Resolution and Order Regarding Rates for Fiscal Year 2019*, Case No. CEPR-AP-2018-0002, at p.1 (May 4, 2018).

[25] *See id.* at pp.1-2 ("These new rates must: .... 5. Address the unique challenges regarding debt service.").

[26] *PREPA's Verified Response and Motion Regarding May 4th Order*, Case No. CEPR-AP-2018-0002, at pp.4, 8-9 (May 11, 2018).

[27] *See, e.g., PREPA's (1) Compliance Filing for Items due August 10, 2018; and (2) Motion to Extend Due Date of Remaining Items*, Case No. CEPR-AP-2018-0002 (August 10, 2018); *PREPA's Second Motion to Extend Due Date of Response to June 22 Order, Item A*, Case No. CEPR-AP-2018-0002 (August 31, 2018); *PREPA's Third Motion to Extend Due Date of Response to June 22 Order, Item A*, Case No. CEPR-AP-2018-0002 (September 17, 2018).

PREPA also took years to actually implement the base rate set in the 2017 Rate Order. On June 28, 2019—two and a half years after the 2017 Rate Order—the Bureau observed that it had created a process for PREPA to "timely implement[] the Permanent Rate and compl[y] with the deadlines established by the Energy Bureau. *PREPA has failed on both accounts.*"[28] Even after the Bureau's admonitions, PREPA continued to seek further extensions that would delay implementation of the new rate. For example, in response to one such motion, the Energy Bureau stated, "[t]he quarterly filings of the rider reconciliations are a vital component of the implementation of the new PREPA rates. As such, PREPA is required to comply with the deadlines and schedules mandated by the Energy Bureau. PREPA has failed to do so, even though it has had ample time to adhere to said deadlines and schedules."[29] PREPA also went on to resist implementation of an energy efficiency rate component in that case, arguing that "any new line item in the customers' bills will generate questions and complains [*sic*]."[30] This reveals PREPA's own political hesitation when it comes to changing rates.

This unfortunate trend continues today, with LUMA following in PREPA's footsteps. Rather than seeking to adjust the base rate, PREPA and LUMA have either cannibalized other funds,[31] or avoided repairs, maintenance, and transformation efforts that stood to benefit all

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[28] *Resolution and Order re: Determination on the Permanent Rates*, Case Nos. CEPR-AP-2015-0001 and NEPR-AP-2018-0003, at p.6 (June 28, 2019) (emphasis added).

[29] *Resolution and Order on PREPA's Request for Extension of Time to Submit Reconciliations for the Month of August 2019*, Case Nos. CEPR-AP-2015-0001 and NEPR-AP-2018-0003, at p.2 (September 13, 2019).

[30] *PREPA's Urgent Motion for Reconsideration of the Timeline for the Implementation of the Energy Efficiency Rider*, Case Nos. CEPR-AP-2015-0001 and NEPR-AP-2018-0003, at p.2 (September 28, 2019).

[31] *See, e.g., Resolution and Order re: Urgent Motion for Budget Revision to Partially Cover PREPA Employee Retirement System Funding for FY2025*, Case No. NEPR-MI-2021-0004, at p.3 (Dec. 26, 2024) (Energy Bureau "not[ing] with concern that PREPA is using non-recurring FEMA reimbursement funds to cover ongoing pension benefit obligations, which reveals a structural deficiency in the system's ability to meet these recurring expenses," and stating that this practice "is neither sustainable nor consistent with sound fiscal management principles").

stakeholders.[32] Indeed, LUMA has admitted to a whole host of initiatives that it has "deferred" for the express purpose of "develop[ing] a budget that is consistent with the 2017 Rate Order," which it incorrectly views as a "financial constraint."[33] "As an example," LUMA writes, "the preventive maintenance and corrective maintenance initiatives have been scaled back to match *available funding*."[34] Available, that is, under an eight-year-old rate. But the funding required to maintain the grid, to harden it against natural disasters, to prevent blackouts, and to pay for financing should determine the rate—not the other way around.

B. The 2017 Base Rate Did Not Include Most Debt Service

As mentioned above, the 2017 Rate Order set a base rate that did not include a debt service component for the vast majority of PREPA's billions of dollars in debt financing. More specifically, when the 2017 Rate Order was entered, the vast majority of PREPA's bond debt was subject to a settlement with PREPA—a settlement that PREPA later abandoned. Had PREPA honored that settlement, the revenue to fund it would have been collected through a "Transition Charge" arising from a separate Energy Bureau proceeding, case CEPR-AP-2016-0001.[35] Because the Transition Charge was being created in a separate proceeding, the Energy Bureau excluded practically all PREPA bond debt (which it referred to as "Participating Debt") from the revenue requirement determined in the 2017 Rate Order and thus from the 2017 base rate.[36] As to the relatively small amount of remaining bond debt assumed not to participate in the settlement and

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[32] *See, e.g., LUMA's Request for Approval of T&D Budgets and Submission of Genco Budgets for FY2025 and Budget Allocations for the Electric Power System*, Case No. NEPR-MI-2021-0004, at "Annual Budgets Fiscal Year 2025" attachment, pp.42-43 (May 25, 2024).

[33] *Id.*

[34] *Id.* (emphasis added).

[35] 2017 Rate Order at p.91.

[36] *Id.* ("In this rate case, the Commission has no jurisdiction to address the Participating Debt.").

therefore included in the base rate, the Energy Bureau rightly noted that Commonwealth law "leaves the [Bureau] no choice" in terms of providing for debt repayment through the base rate, including all principal and interest payments,[37] as well as a debt service coverage ratio that it set at 1.40, above the 1.20 ratio required by the Trust Agreement.[38]

Importantly, the Energy Bureau explicitly rejected arguments from certain intervenors that "PREPA's debt is too high and should be renegotiated [further] downward."[39] It noted that "PREPA has already obtained from bondholders a 15% reduction in principal, lower interest rates and a five-year deferral of principal" under the then-extant settlement.[40] The Energy Bureau found there was "no evidence" that the settlement was unfair to PREPA or that PREPA should have negotiated differently.[41]

Given the then-pending Transition Charge that would have covered most bond debt, the Energy Bureau's exclusion of such debt from the revenue requirement in 2017 may have made practical sense. But National recognized and flagged the problems that could, and ultimately did, arise from excluding most bond debt from the base rate. *First*, foreseeing delays in the rate review

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[37] *Id.*; *see also, e.g.*, Act 4-2016, § 9(c) ("The Commission shall approve a rate that [] is sufficient to guarantee the payment of principal, interest, reserves, and all other requirements of bonds and other financial obligations that have not been defeased as part of the securitization provided in Chapter IV of the Electric Power Authority Revitalization Act."); *In re Fin. Oversight & Mgmt. Bd.*, Case No. 18-00021-LTS, Doc. No. 1, *Verified Adversary Complaint of the Puerto Rico Energy Commission*, at ¶ 14 (D.P.R. Mar. 4, 2018) (predecessor to Energy Bureau stating that it "must 'prevent its actions from impairing PREPA to meet its contractual obligations to bondholders,'" and thus "Commission-set rates must produce revenues sufficient 'for the payment of the principal of and interest on PREPA's bonds'" (alterations adopted)).

[38] 2017 Rate Order at pp.93-94. Notably, PREPA's own expert argued for an even higher debt service coverage ratio of 1.57-2.00, reasoning that this higher level would allow PREPA to regain access to the credit market at a higher AA rating. *Id.* at p.94. During its Title III case, however, PREPA has not used any revenues—including those related to the debt that was included in the base rate—for debt service.

[39] *Id.* at p.94.

[40] *Id.* at p.95.

[41] *Id.*

and implementation process, National requested a temporary rate adjustment early in the rate case to bridge the gap until a new base rate was implemented.[42] National described how PREPA had not adjusted its base rate since *1989*, leading to "an unnecessary and harmful crisis of its own making."[43]

Second, National expressed concern to the Energy Bureau about the revenue requirement excluding bond debt and recommended that all bond debt be included, with any downward revisions resulting from the settlement to occur later.[44] While the Bureau acknowledged that all debt "must be covered by its rates," it reasoned that the executed settlement exempted PREPA from including such debt in the revenue requirement until the Transition Charge was finalized.[45] Critically, the Bureau relied on "a common overall expectation recognized by PREPA and intervenors participating in this proceeding that *the restructuring of the debt, as set forth in the RSA [settlement], will proceed.*"[46]

PREPA violated that expectation. On July 2, 2017, just six months later, the FOMB filed a Title III bankruptcy petition on behalf of PREPA and reneged on the settlement (much as it

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[42] *See National's Petition for Rate Review and Establishment of Temporary Electricity Rate*, Case No. __ (Sept. 17, 2015), and *Affidavit of Timothy R. Coleman*. While a copy of these filings could not be located on the Energy Bureau's website, National will provide a stamped copy upon request.

Unfortunately, National's petition was denied. *See Resolution re: Order to Show Cause; Rate Review; Temporary Rate*, Case No. CEPR-QR-2015-0002 (Oct. 1, 2015).

[43] *Id.* at p.3.

[44] *See* 2017 Rate Order at pp.215-16.

[45] *Id.* at p.216 n.351.

[46] *Id.* (emphasis added).

would renege on later settlements).[47] This action rendered the 2017 base rate's exclusion of most debt service an anomaly—one that has lingered for eight years in defiance of Commonwealth law.

C. The Energy Bureau Initiates This Rate Review in Mid-2023

On June 30, 2023, the Energy Bureau ultimately initiated this Rate Review, which it indicated would proceed in three phases.[48] The scope of the Rate Review is broad: To "cover the full scope of revenues and expenditures involved in providing electric service in Puerto Rico."[49] On March 15, 2024, the Energy Bureau issued a Resolution and Order setting forth an "Expected High-Level Timeline" for the Rate Review, pursuant to which LUMA would have filed by June 1, 2024 a proposed revenue requirement to inform PREPA's future base rate.[50] In that order, the Energy Bureau emphasized that the FOMB had filed and sought confirmation of a proposed plan of adjustment concerning PREPA's debt and pension obligations, and that following confirmation of its proposed plan, PREPA and the FOMB would submit the resulting information to the Energy Bureau to factor into a new rate.[51]

On April 12, 2024, the Energy Bureau set aside the above schedule, noting the recent plan confirmation proceedings and stating, "[t]he Title III Court's final decision on the Amended Plan will directly affect this proceeding because, once confirmed, future electricity rates will need to incorporate a Legacy Charge (as may be amended or modified), while also funding the operators

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[47] *In re Fin. Oversight & Mgmt. Bd.*, Case No. 17-04780-LTS, Doc. No. 1, *Title III Petition for Covered Territory or Covered Instrumentality* (D.P.R. July 3, 2017).

[48] *See Resolution and Order re: Initiating Rate Review*, Case No. NEPR-AP-2023-0003, at p.2 (June 30, 2023).

[49] *Resolution and Order re: Preliminary Guidance on Rate Case Procedures and Notice of Upcoming Conference*, Case No. NEPR-AP-2023-0003, at p.1 (Dec. 16, 2024) ("Dec. 16 Order").

[50] *Resolution and Order re: Guidance for Phase 2 Rate Review Filing and Scheduling of Technical Conference*, Case No. NEPR-AP-2023-0003, at p.6 (Mar. 15, 2024).

[51] *See id.* at pp.1-3.

of Puerto Rico's electricity system – PREPA, LUMA, and Genera – and PREPA's pension obligations."[52] In short, the Energy Bureau decided to pause the Rate Review "until the Title III Court has rendered its decision on the confirmation of the Amended Plan,"[53] apparently reasoning that the FOMB's proposed plan would soon be confirmed, and the rate would be set accordingly.

The FOMB's plan was not confirmed. Instead, two months later, the United States Court of Appeals for the First Circuit issued an opinion reversing key holdings of the Title III court on which the FOMB's proposed plan of adjustment was based.[54] The First Circuit vindicated the Bondholders' longstanding position, finding that they hold a perfected, secured lien on all of PREPA's Net Revenues. Despite two subsequent attempts by the FOMB to overturn the First Circuit's decision, it remains binding on the Title III court and, in the Bondholders' view, precludes confirmation of the previously proposed plan (as the FOMB has effectively admitted by indicating it intends to file another proposed plan), or of any similar plan that massively impairs the Bondholders while allowing unsecured creditors to jump the creditor line.

For the next six months, apart from a couple of information responses from LUMA, there were no public filings or orders in the Rate Review. Then, on December 10, 2024, the Energy Bureau clarified that its consultants had engaged in preliminary discussions with "relevant parties" to establish the filing requirements for the Rate Review, and that it expected to finalize the requirements by early February 2025.[55] Later that month, the Energy Bureau issued additional

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[52] *Resolution and Order re: Milestones and Deadlines*, Case No. NEPR-AP-2023-0003, at pp.2-3 (Apr. 12, 2024).

[53] *Id.* at p.3.

[54] *See In re Fin. Oversight & Mgmt. Bd.*, 104 F.4th 367 (1st Cir. June 12, 2024), *subsequently amended*, 121 F.4th 280 (1st Cir. Nov. 13, 2024).

[55] *Resolution and Order re: Notice of Upcoming Rate Filing Requirements*, Case No. NEPR-AP-2023-0003, at p.1 (Dec. 10, 2024).

orders regarding Rate Review procedures and scheduled technical conferences for December 20, 2024 and January 10, 2025.[56]

At the Jan. 10 Conference, the Energy Bureau's consultants and the operators discussed various matters. As particularly relevant to the Bondholders, the discussion turned to the amount of PREPA's outstanding bond obligations for use in the revenue requirement, which will inform a new base rate. That topic, among others, was also raised in the consultants' Jan. 3 Questions and Jan. 10 Questions. As such, Dr. Asa Hopkins invited the Bondholders to weigh in. This submission follows.

DISCUSSION

I. The Revenue Requirement Must Consider "All Costs and Revenues," Including PREPA's Existing Bond Debt

The Energy Bureau has repeatedly recognized—including as recently as December 20, 2024—that the Rate Review must consider "all costs," "regardless of source or payee."[57] The Bureau's guidance is clear that "all" means all. And that makes perfect sense, because the revenue requirement is meant to represent PREPA's entire cost structure, in turn allowing for design of an appropriately compensatory rate.

Nonetheless, the consultants' questions have raised the possibility of treating PREPA's bond debt differently, as something less than "all." In the Jan. 3 Questions, the consultants directed LUMA to "reflect in its proposed revenue requirement, the most recent settlement offer made by the FOMB. While not a final figure, the FOMB offer is more representative of the likely debt

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[56] *See* Dec. 16 Order; Dec. 20 Order.

[57] Dec. 20 Order at p.3; *see also, e.g., id.* (Rate Review will consider "information about *all costs*" (emphasis added)); Dec. 16 Order at p.1 ("All expenditures means all expenditures for normal operations, storm resilience and restoration, Puerto Rico Electric Power Authority ('PREPA') owned infrastructure, *and anything else*." (emphasis added)); *id.* at p.3 (Rate Review will involve "[c]omplete financial mapping of *all ... expenditures*" (emphasis added)).

amount than is the number zero."[58] In the Jan. 10 Questions, the consultants asked which of five possibilities should be used to represent PREPA's bond debt in the revenue requirement:

1. Zero, on grounds that we don't know the number yet.
2. FOMB's latest settlement offer that is publicly available.
3. The full face amount of legacy debt plus accrued interest.
4. Halfway between the FOMB's position and the bondholders' claim.
5. Other?

Jan. 10 Questions at p.2. And in the Jan. 10 Conference, an additional possibility was raised: Using the FOMB's proposed treatment of some group of bondholders in its now-defunct 2024 plan of adjustment.[59]

The only appropriate and lawful calculation of PREPA's bond debt, for purposes of establishing the revenue requirement, is a modified version of #3 above: The full face amount of bond debt plus accrued interest, *plus* the mandatory 1.20 debt service coverage ratio ("DSCR").[60] This amount is readily determinable as depicted on the following page:

[58] Jan. 3 Questions at p.4.

[59] Jan. 10 Conference at 1:00:38 to 1:04:16.

[60] A 1.20 DSCR is actually less than what the Energy Bureau used in the 2017 Rate Order (1.40), and still less than what PREPA's own experts advocated in that case (1.57 to 2.00). *See supra* pp.8-9 & n.38.

Principal Amount	$8.259 billion
Pre-Petition Interest	$0.218 billion
Post-Petition Interest[61]	$3.690 billion
Total	**$12.166 billion**
Illustrative Annual Level Debt Service[62]	$772 million / year
With 1.20 DSCR	**$926 million / year**

The full face amount of the bond debt should be used because, as the First Circuit concluded, that is the "proper amount" of the debt.[63] The First Circuit rejected the argument that the proper amount is something less. Thus, that is the amount PREPA legally owes at this time, just as a 1.20 DSCR is legally mandated at this time.

To be clear, the bondholders are not contending that the above numbers will necessarily be the outcome of the Title III (or any other) legal proceedings. As the consultants have noted, "we don't know th[at] number yet," because proceedings remain ongoing.[64] But in determining the revenue requirement, it is not the Energy Bureau's role or mandate to handicap PREPA's costs based on speculation about the outcome of ongoing litigation. Doing so would usurp the role of the Title III court, prejudge the outcome, and amount to the Bureau taking restructuring into its own hands.[65] Rather, as the Energy Bureau has stated, it must simply consider "all costs."

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[61] For illustrative purposes only, using an assumed effective date of June 30, 2025. Following the First Circuit's ruling, there is no controversy that PREPA bondholders are owed "roughly $8.5 billion." *In re Fin. Oversight & Mgmt. Bd.*, 121 F.4th at 312. The bondholders' entitlement to post-petition interest will need to be determined by the Title III court or an appellate court.

[62] For illustrative purposes only, assuming a 6% interest rate and a 50-year term.

[63] *In re Fin. Oversight & Mgmt. Bd.*, 121 F.4th at 312.

[64] Jan. 10 Questions at p.2.

[65] Whether to make any reduction to PREPA's bond debt—for affordability reasons or otherwise—is within the exclusive jurisdiction of the Title III court. In responding with their views regarding the consultants' questions here, the Bondholders reserve all rights to litigate and appeal such issues in the appropriate forum(s).

PREPA's bond debt is one of those costs, and it must be considered as it stands now. If the cost of PREPA's bond debt is reduced at some future time, then the Energy Bureau can readily adjust the rate accordingly.[66]

This approach to calculating PREPA's bond debt for the revenue requirement is also consistent with how the Energy Bureau's consultants are calculating other costs. When it comes to LUMA and Genera's fees and bonuses, for instance, the consultants have stated, "[t]he filed budgets should include the fixed fee and 100% of the performance metrics award."[67] Of course, it is unknown whether LUMA or Genera will actually earn 100 percent (or any percent) of their performance-based incentive bonuses, and it is unknown whether LUMA and/or Genera will even continue to earn their fixed fees, given that some politicians have suggested terminating operator agreements. Notwithstanding these uncertainties, the consultants have asked for the full fee and bonus amounts to be included for consideration in the revenue requirement. It is no different for PREPA's bond debt.

Considering the full amount of PREPA's bond debt in the revenue requirement is not only consistent with the Energy Bureau's statements in its Dec. 16 and Dec. 20 Orders as well as the consultants' calculation of other costs, it is also consistent with Commonwealth law and the Bureau's 2017 Rate Order. The following Commonwealth laws are illustrative:

- **Act 4-2016, § 9(c):** "The Commission shall approve a rate that [] is **sufficient to guarantee the payment of principal, interest, reserves, and all other requirements of bonds and other financial obligations** that have not been defeased as part of the securitization provided in Chapter IV of the Electric Power Authority Revitalization Act."

[66] For example, the Energy Bureau routinely reconciles portions of PREPA's rate to true up projected with actual costs for fuel and purchased power—showing that the Bureau is experienced with and has procedures in place to reconcile rates when necessary.

[67] Jan. 10 Questions at p.3.

- **Act 57-2014, § 6.25:** "The Bureau **shall approve a rate that (i) allows electric power service companies to recover all ... financing costs ...**"

- **Act 57-2014, § 6.25(b):** Providing that during a rate review, the Energy Bureau shall consider "**the expenditures related to the Authority's debt repayment.**"

- **Act 57-2014, § 6.3(p):** Providing that it is the Energy Bureau's duty to "[e]nsure that the powers and authorities exercised by PREB over [PREPA] ... including those related to rate review and approval, **guarantee that [PREPA] meets its obligations to bondholders.**"

- **Act 83-1941, § 5(l):** "The Authority is hereby conferred, and shall have and exercise, the rights and powers .... To propose and collect just, reasonable, nondiscriminatory rates and fees ... **that are sufficient to cover reasonable expenses incurred by the Authority ... for the payment of the principal of and interest on its bonds**, and for fulfilling the terms and provisions of the agreements entered into with or for the benefit of purchasers or holders of any bonds of the Authority and other creditors." (emphasis added).[68]

These laws make clear that rates must be sufficient to cover existing debt. They do not allow the Energy Bureau to *sua sponte* reduce the cost of debt service based on speculation about the possible outcome of legal proceedings in another forum(s).

As discussed in the Background section, the Bureau's 2017 Rate Order likewise recognized that debt service must be included in the revenue requirement. It rightly noted that Commonwealth law "leaves the [Bureau] no choice" in terms of providing for debt repayment through the base rate.[69] That observation remains true today.

For these reasons, the Bondholders object to any arbitrary reduction in the amount of bond debt that is considered for the revenue requirement in this Rate Review, whether that be to zero, to the FOMB's latest settlement offer, to the FOMB's defunct 2024 proposed plan of adjustment,

[68] Under Section 8(f) of Act 120-2018, the private operators are similarly "required to meet the requirements imposed on PREPA or any other Electric Service Company ... to increase or reduce such duties, rents, and rates."

[69] 2017 Rate Order at p.91.

to "halfway," or to any other amount that is less than the full amount set forth in the table on page 15. "All costs" means all costs.

II. There Is No Basis for Adopting So-Called Alternative Budgets, Which Would Arbitrarily Reduce PREPA's Ability to Recoup Costs

Compounding the problem discussed in Part I above, the Energy Bureau's consultants have also proposed creating multiple budgets reflecting significant reductions—as much as *-75 percent*—to the all-in budget. First, there would be an "optimal" budget, which "would reflect all actions and all associated costs" that are deemed necessary and include "all the expenses and expenditures" of the system.[70] In other words, a normal budget.

But then, there would be one or more "alternative" budgets. These alternative budgets "would reflect spending levels producing base rate increases of, respectively, 75%, 50%, and 25% of the rate increase associated with the optimal budgets."[71] The consultants later proposed still other alternative budgets, including one based on "the rate increase that the submitter deems appropriate," and unspecified "other options."[72] These alternative, hacked-down budgets are explicitly driven by one consideration—the desire to avoid rate increases beyond a purported level that "citizens are willing to pay."[73]

The Bondholders are not aware of a basis in governing law for the Energy Bureau to make seemingly arbitrary 25 to 75 percent reductions in PREPA's ability to recoup its costs. Indeed,

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[70] Jan. 3 Questions at p.2.

[71] *Id.*

[72] Jan. 10 Questions at p.2. The consultants also raised the possibility to "phase in" rate increases—even at a reduced level. Jan. 3 Questions at p.3.

[73] Jan. 3 Questions at p.2; *see also* Jan. 10 Conference at 1:40:41 to 1:41:01 ("We have on the table four possible options for how to handle the question that we raised, which is how to address the possibility that the optimal budget will produce a rate that nobody thinks they want to be, frankly, associated with.").

Section 6.25(b) of Act 57-2014 sets out a long list of data for the Bureau to consider during a rate review, including debt service, direct and indirect costs related to the generation and transmission and distribution systems, fuel costs, energy efficiency costs or savings, the cost of subsidies, and more. The law's data-driven, comprehensive process is meant to align rates with costs. Hacking chunks off the budget would do the opposite—it would misalign rates and costs, driving PREPA deeper into dysfunction.

Further, if the Energy Bureau were to proceed with *both* an improper reduction to the bond debt amount *and* an alternative budget, those errors would be seriously compounding. To illustrate, assume the Bureau reduced the bond amount by 50%, put the resulting figure into the "optimal" budget, and then selected the -50% alternative budget—the final result would be a revenue requirement reflecting *only 25%* of the debt cost. The Bondholders strongly disagree with each of these approaches independently, but they are even worse together.

Finally, the Bondholders note that the consultants suggested the alternative budgets could help the Energy Bureau "explain [rates] to the public."[74] To the limited extent the consultants intend to use the alternative budgets only for illustrative/explanatory purposes to show service quality at various rate levels, the Bondholders are not necessarily opposed to them collecting such information. Or, to the extent the Energy Bureau were to reduce the "optimal" budget on a principled basis supported by the record and the law—for example, if it found that an operator had miscalculated or improperly inflated a cost—that could also be appropriate. But arbitrarily reduced budgets should not form the basis for the revenue requirement in this Rate Review.

WHEREFORE, the Bondholders respectfully request that the Energy Bureau and its consultants **TAKE NOTICE** of this information.

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[74] Jan. 3 Questions at p.3.

RESPECTFULLY SUBMITTED,

THIS 17th DAY OF JANUARY 2025

CERTIFICATE OF SERVICE: We hereby certify that the foregoing brief will be submitted in person at the Energy Bureau for filing via the Electronic Filing System, and courtesy copies were sent via electronic means to:

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