

Subcommittee on Indian, Insular and Alaska Native Affairs

Doug LaMalfa, Chairman

Hearing Memorandum

March 20, 2017

To: All Subcommittee on Indian, Insular and Alaska Native Affairs Members

From: Majority Committee Staff,
Subcommittee on Indian, Insular and Alaska Native Affairs

Hearing: Oversight Hearing on “*The Status of the Puerto Rico Electric Power Authority (PREPA) Restructuring Support Agreement.*”

On Wednesday, **March 22, 2017, 10:00am in 1324 Longworth House Office Building**, the Indian, Insular and Alaska Native Affairs Subcommittee will hold an oversight hearing on “*The Status of the Puerto Rico Electric Power Authority (PREPA) Restructuring Support Agreement.*”

Policy Overview

- The current PREPA debt sits at roughly **\$8.9 billion** spread across four classes: uninsured legacy bonds (\$5.6 billion), insured legacy bonds (\$2.1 billion), relending bonds (\$0.4 billion), and bank debt (\$0.7 billion).
- The current PREPA Restructuring Support Agreement (RSA) is set to expire on **March 31, 2017**. It has been extended 15 times since terms were first agreed to in December 2015.
- The PREPA RSA will help address how the utility will be able to meet its debt obligations by lowering the overall debt burden, lowering total debt service, providing a 5-year period of principal relief, and allowing for reinvestment in PREPA’s aging infrastructure.
- The PREPA RSA requires certain structural reforms within PREPA that are vital for the utility to begin de-politicizing rate structures in order to operate efficiently and provide stable, consistent and affordable power generation.
- PREPA has a major bond payment of roughly \$455 million of combined principal and interest¹ due on July 1, 2017. Without the cash flow relief provided by the terms of the RSA and without any other viable options for making such a payment afforded to the distressed utility, PREPA will once again default and residents of the island may experience interruptions in services.

¹ \$237 million of principal, \$218 million of interest.

Invited Witnesses

Panel I

The Honorable Ricardo Rosselló
Governor of Puerto Rico
San Juan, Puerto Rico

Accompanied by:
Mr. Gerardo Portela-Franco
Executive Director
Puerto Rico Fiscal Agency and Financial Advisory Authority

Panel II

Mr. José B. Carrión III
Chairman
Financial Oversight and Management Board of Puerto Rico
San Juan, Puerto Rico

Mr. Luis Benítez Hernández
Chairman
PREPA Governing Board
San Juan, Puerto Rico

Mr. Stephen Spencer
Managing Director
Houlihan Lokey
Minneapolis, Minnesota
On behalf of Franklin Advisers, Inc. and OppenheimerFunds Inc.

Mr. Adam Bergonzi
Managing Director & Chief Risk Officer
National Public Finance Guarantee Corporation
Purchase, New York

Mr. Rob Bryngelson
President & CEO
Excelerate Energy L.P.
The Woodlands, Texas

Ms. Ana J. Matosantos
Member
Financial Oversight and Management Board of Puerto Rico
Sacramento, California

Background

The Puerto Rico Electric Power Authority (PREPA) is the primary power utility operating in the territory, providing power generation to the 3.4 million Americans residing on the island. Formed in 1941, PREPA is a public corporation with approximately 9,550 employees, 33 customer service offices, 29 technical service offices, and 38 local offices serving seven regions encompassing the island. PREPA is directed by a Governing Board comprised of nine members, seven of whom are appointed by the Governor with approval by the Puerto Rico Senate. The other two board members are elected by the consumer community under an election supervised by the Consumer Affairs Department. Among the structure of PREPA there are anywhere from 150-300 “confidence employees” that are direct political appointments made by the Governor. These coveted patronage jobs are often held by individuals who are unqualified in the areas of expertise required to hold these positions, contributing to the inefficiency of operations within PREPA.²

On February 16, 2016, the Legislative Assembly of Puerto Rico enacted, and the Governor of Puerto Rico Alejandro Garcia Padilla signed into law, Act 4-2016, known as the PREPA Revitalization Act. As a condition of the Act and in an effort to de-politicize the Governing Board, a third party consulting firm was brought in to source industry professionals with experience in operating and managing major utility companies. Governor Garcia Padilla appointed these new members in November 2016 with the goal of establishing an independent, non-partisan Governing Board with the relevant experience and industry expertise necessary to make the structural changes within the utility in order to increase managing efficiency.

The new independent PREPA Board reviewed and approved the RSA in January of 2017 and was continuing negotiations with creditors on finalizing the RSA. However, under the new Rosselló Administration, the task of negotiating the RSA with the creditor community has shifted from the hands of the independent PREPA Governing Board to the Puerto Rico Fiscal Agency and Financial Advisory Authority (AAFAF). The PREPA Board’s fate under the new Rosselló Administration remains unclear.

How the RSA Works

The basics of the PREPA RSA contemplate a consensual exchange of roughly \$5.6 billion in uninsured legacy power revenue bonds for \$4.8 billion in securitization bond debt. This equates to about a 15% haircut for creditors in exchange for more secure bonds backed by a 3-cent per kilowatt-hour transition charge that will be covered by PREPA’s consumers. Also included in the details of the RSA is a 5-year period of principal relief that will allow PREPA to direct funds that would otherwise be used for debt service towards investing and updating their

² For an in-depth review on operations within PREPA consult the Committee memo from January 11, 2016 Oversight hearing, “*Exploring Energy Challenges and Opportunities Facing Puerto Rico.*” http://naturalresources.house.gov/uploadedfiles/emr_hearing_memo_1_12_16.pdf

aging infrastructure. This is critically important given the recent episodes involving severe failures in PREPA's outdated and unmaintained system which has resulted in massive power outages for the residents of the island.³

RSA Under Review by the Governor

Governor Rosselló has stated that his new Administration requires time to review the RSA upon taking office in January of 2017, with the Ad Hoc Group of creditors agreeing to extend the RSA deadline to March 31, 2017. The review of the RSA by the Governor's advisors at AAFAF has led to continuing negotiations between the Government and creditors, with the Governor indicating that he is hoping to negotiate a better deal within the existing framework.⁴

The Oversight Board established under PROMESA (P.L. 114-187) has indicated their support for the Governor's efforts to gain more from continuing negotiations of the RSA by way of deeper concessions from creditors.⁵ The creditor community has indicated that it is willing to make further adjustments to the RSA in order to improve the terms in favor of the island, in order to reach a final agreement with Governor Rosselló. However, those parties negotiating have also made clear to the Governor and AAFAF that any major changes to the pre-existing RSA or any substantial attempts to re-negotiate the terms of the deal will not be entertained.

Vital Infrastructure Projects at Stake

Included in the details of the RSA is the ability for PREPA to invest the newly established savings on the debt obligation in modernizing the power infrastructure. A primary example of this is the Aguirre Offshore GasPort (AOGP). Exceleerate Energy has invested \$10 million in trying to bring this project online in order to help PREPA diversify their power generation and begin the necessary transition away from the utility's high dependence on fossil fuels which has resulted in an inefficient productivity and an increase in energy prices. The AOGP will not only meet Federal Mercury and Air Toxic Standards (MATS) compliance but it also has the potential to help PREPA lower energy costs into the future. Proponents of the RSA note that in order for PREPA to have the necessary capital to bring the AOGP project online by 2018 as currently scheduled an agreement between the Governor and the creditors must be reached on the RSA.

³ In September of 2016, an overheated power switch caused a 2,000-gallon mineral oil tank to explode at the Aguirre power plant in the south of the island. The ensuing blackout left 1.5 million residents without power for days, shutting down schools and businesses. The severity of the episode led Governor Alejandro García Padilla to activate the National Guard and declare a state of emergency.

⁴ Brown, Nick. "Puerto Rico governor says he wants to improve, not 'destroy,' PREPA restructuring." Reuters. Thomson Reuters, 13 Mar. 2017. Web. 17 Mar. 2017. <<http://www.reuters.com/article/us-puertorico-debt-governor-idUSKBN16K2PE?mod=related&channelName=politicsNews>>.

⁵ Brown, Nick. "Puerto Rico oversight board approves revised government turnaround plan." Reuters. Thomson Reuters, 13 Mar. 2017. Web. 17 Mar. 2017. <<http://www.reuters.com/article/us-puertorico-debt-idUSKBN16K1WG>>.