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BANK AND CHAIRMAN OF THE BOARD OF THE PUERTO RICO FISCAL AGENCY
AND FINANCIAL AUTHORITY, GOVERNMENT OF PUERTO RICO

**Written Statement of Christian Sobrino Vega
May 8, 2018**

This statement is submitted on behalf of Mr. Christian Sobrino Vega, President of the Government Development Bank and Chairman of the Board of the Puerto Rico Fiscal Agency and Financial Advisory Authority (known by its Spanish acronym, AAFAF). Mr. Sobrino also acts as the Chief Advisor for Economic Development to the Governor of Puerto Rico, is the Governor's designee on the Financial Oversight and Management Board for Puerto Rico, and is AAFAF's representative on the Governing Board of the Puerto Rico Electric Power Authority (PREPA). Mr. Sobrino's statement addresses the transformation of Puerto Rico's energy sector and the future of Puerto Rico's electric system.

Overview of Puerto Rico's Vision for the Future of Electric System

On January 23, 2018, Governor Rosselló announced a vision for the transformation of PREPA and the Island's electric system to a modern, reliable, and resilient system that can provide electricity at affordable rates to customers. The envisioned transformation is based on attracting private participation to the sector through a concession of the transmission and distribution system and private ownership and/or operation of the generating capacity. The transformation is desperately needed.

While Hurricanes Irma and Maria left the electric system in shambles and millions of Puerto Ricans without electricity for months, the fragile nature of the Island's electricity infrastructure was painfully evident before the September devastation. PREPA's infrastructure was practically abandoned in the last decade and the generation assets are on average approximately 28 years older than the industry average in the mainland United States. As a result, the people of Puerto Rico have been shouldering unacceptably high electricity costs for unreliable electric service for years.

The envisioned transformation is intended to bring to Puerto Rico a consumer-centered and innovative model that provides people with options, is sustainable, uses advanced technology, and is resilient to the ravages of nature. Establishment of an independent regulator and a regulatory structure that creates investor and customer confidence is critical. The transformation is also intended to be an innovative energy model, with a commitment to the use of renewable and environmentally-friendly resources and with the goal of achieving more than 30% renewable energy generation and an energy cost of less than 20 cents per kilowatt hour. With an efficient, reliable, and modern electric power system, Puerto Rico will attract new industries and businesses that create jobs, which will add value to our society, as well as allow for greater competition in energy generation on the Island. Energy transformation will provide a springboard for the modernization of Puerto Rico.

Process to Achieve Energy Sector Transformation

Governor Rosselló has set forth a three-phase plan for the transformation of the electric sector. The first phase will define the framework for the transformation through legislation. The second

phase will involve marketing, receiving offers from interested parties, and evaluating the technical, economic, and financial capabilities of offerors. In the final phase, the terms of awarding and hiring the selected parties that meet the requirements for the transformation and modernization of our energy system will be negotiated, finalized, and approved.

The Government intends the transformation process to be achieved through a proven model – Puerto Rico’s Public-Private Partnership Act (PPP Act). The PPP Act is well-understood by potential investors and has been used successfully in the Luis Muñoz Marín International Airport concession, the concession of certain toll roads, and multiple other infrastructure projects in Puerto Rico. The legal framework is one that promotes a competitive process and assures transparency and fairness while still providing the flexibility necessary to achieve the best results for Puerto Rico. I also expect that the transaction will be approved by the Title III Court having jurisdiction over PREPA in its pending insolvency proceeding.

The assumed “base case” for the contemplated transformation involves (i) private ownership and/or operation of all generation assets and a development of greenfield generation projects with a focus on a diversified fuel mix and clean energy and (ii) a private operator of the transmission and distribution system through a concession model, which leaves the ownership of the assets in public hands under the operation of a private operator. I anticipate this “base case” will be subjected to a market test in order to determine the extent of investor interest and whether higher values and/or better transaction terms can be achieved by using an alternative structure. I anticipate the timeline to run the competitive process for the transformation will be at least 12 to 18 months.

In any structure, federal funding provided for permanent system improvements will be necessary to achieve the appropriate levels of resiliency and hardening of the system consistent with the purposes of the Robert T. Stafford Disaster Relief and Emergency Assistance Act of 1988. The structure of the transformation will be designed to assure that benefits of federal funding flow to the citizens – just as in any natural disaster.

In a joint effort with the federal government to make the Island’s recovery efforts the most transparent, effective, and efficient in U.S. history, the Governor created the Central Recovery and Reconstruction Office of Puerto Rico (CRRO) within the Public Private Partnership Authority. The CRRO is responsible for the development and implementation of a strategic plan for the reconstruction of Puerto Rico in the short, medium, and long term. In addition, the CRRO is intended to provide financial accountability during the transformation process. The CRRO has the power to approve audit policies and establish its own governmental ethics processes to govern all projects related to the reconstruction.

Role of Independent Regulation

Independent regulation is essential to the transformation and modernization of Puerto Rico’s electric sector, just as it is on the mainland. An independent regulatory framework is necessary to support the desired power sector transformation, create investor confidence, and implement stable and accepted modes of regulation and economically-efficient rates. The current regulator

and regulatory structure, which were designed to regulate a public monopoly, cannot achieve those objectives without modification.

During the transformation process, I anticipate that a new or modified, adequately funded, and independent regulator will be established by the Puerto Rico legislature. I expect this regulator will be comprised of highly-qualified members with staggered terms to mitigate against political interference. This regulator will be free from regulatory conflicts and structured to support the steps leading to sector transformation. I expect this commission to be supported by a staff with utility regulation expertise, and that the ratepayer advocate will exist separately from the regulator to provide an independent voice for consumers.

After the transformation has been completed with a successful transaction, the new regulatory structure will protect consumers and implement Puerto Rico's energy sector public policy. It must do that while creating investor confidence and attracting private capital. To accomplish those goals, the new regulatory structure, while being tailored to the situation in Puerto Rico, should also incorporate known structures and established standards used by other economically-developed jurisdictions to both protect customers and regulate viable private sectors.

Importance of Energy Transformation to Puerto Rico's Economic Recovery

Transformation of the energy sector is a vital part of Puerto Rico's economic recovery. Certain statistics suggest that electric bills for similar amounts of electricity in Puerto Rico can be twice the mainland numbers. The high cost of electricity in Puerto Rico is punishing for our citizens and a major inhibitor to attracting businesses to the Island. It is our belief that the improvement of the power grid will have a strong positive impact on long-term economic growth. The Government's economists inform us that empirical analysis from Argentina and other countries indicates that a 1% increase in investment will increase gross domestic product per capita by 0.3%, implying that consistent investment results in considerable increases in GNP levels over time. In the recently-certified fiscal plan for PREPA, the Oversight Board projected that the energy reforms would increase growth by 0.30% starting in FY2020. As a result, electric sector reform is one of the lynchpins of the future of Puerto Rico.