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BY ELECTRONIC MAIL

December 28, 2022

Mr. Fermín Fontanés Gómez
Executive Director
Puerto Rico Public Private Partnerships Authority

Re: Genera PR, LLC

Dear Mr. Fontanés Gómez,

In accordance with the contract review policy of the Financial Oversight and Management Board for Puerto Rico ("FOMB") established pursuant to Section 204(b)(2) of PROMESA, we have reviewed the proposed Thermal Generation Facilities Operation and Maintenance Agreement between (i) the Puerto Rico Public Private Partnerships Authority (the "P3A"), as Administrator, and the Puerto Rico Electric Power Authority ("PREPA"), as Owner; and (ii) Genera PR, LLC, as Operator (the "Proposed Contract").

After reviewing the Proposed Contract, the FOMB concludes "Approved with Observations." Observations related to the Proposed Contract are set forth in Appendix A attached hereto.

Our review is solely limited to compliance of the Proposed Contract with Section 204(b)(2) of PROMESA, which seeks to ensure proposed contracts promote market competition and are not inconsistent with approved Fiscal Plans. For the avoidance of doubt, the review performed by the FOMB does not cover a legal review of the contractual documentation or the contracting process, including without limitation: (i) compliance with contracting requirements under applicable laws, rules, and regulations, both federal and local; and (ii) compliance with applicable laws, rules, and regulations governing procurement activities, both federal and local.

In addition, the FOMB has not engaged in any due diligence or background check with respect to the contracting parties nor whether the contracting parties comply with the requirements under the applicable contract. Any material changes to the Proposed Contract must be submitted to the FOMB for review and approval **prior to execution**.

This letter is delivered as of the date hereof and we reserve the right to provide additional observations and modify this letter based on information not available when the review was conducted. In addition, during the course of our review, we may receive information which we may refer to the relevant authorities.

This letter is issued only to the P3A and solely with respect to the Proposed Contract.

Sincerely,

Jaime A. El Koury
General Counsel

PUERTO RICO PUBLIC PRIVATE PARTNERSHIPS AUTHORITY/PUERTO RICO ELECTRIC POWER AUTHORITY – GENERA PR, LLC

Fiscal Plan Alignment

This review covers the Proposed Contract between (i) the P3A, as Administrator, and PREPA, as Owner; and (ii) Genera PR, LLC as Operator (the "Operator").

The Proposed Contract stems from a competitive procurement process consisting of three stages: (i) market sounding; (ii) Request for Qualifications (RFQ); and (iii) Request for Proposals (RFP) executed by the Partnership Committee designated by the P3A.[1]

On December 2, 2019, the P3A issued a letter requesting private sector feedback on the transformation of PREPA's electric generation operations. On August 10, 2020, the Partnership Committee issued an RFQ pursuant to Section 5 of Act 120-2018 and Section 3 of Act 29-2009 and received a total 15 Statements of Qualifications (SOQs), each from different respondents. The submitted SOQs were evaluated to determine which respondents met the minimum requirements necessary to carry out the operation and maintenance services, in compliance with Act 120-2018 and Act 29-2009. In particular, respondents were evaluated on: (i) their capability and experience operating, maintaining, managing and undertaking selected maintenance capital projects as needed for thermal generation facilities with capacity in excess of 100 MW, which operate on natural gas and/or fuel oil; (ii) their financial stability and resources; (iii) asset management expertise, primarily related to fuel procurement and management; (iv) strong technical expertise, with a track record of high-quality safe and reliable operations; (v) experience and demonstrated ability to manage a largely Spanish-speaking workforce; (vi) experience operating within, and complying with, local community standards; (vii) experience complying with regulatory and permitting approvals; and (viii) experience with decommissioning, or subcontracting and overseeing the decommissioning of thermal generation plants. Out of the 15 submitted SOQs, the Partnership Committee identified 8 respondents as Qualified Respondents, including the Operator, and invited them to participate in the RFP process.

The RFP was issued by the Partnership Committee on November 10, 2020, and a total of two proposals were received from the Qualified Respondents on December 22, 2021. After allowing the two proponents to resubmit updated proposals by March 21, 2022, the Partnership Committee evaluated these using the following criteria: (i) Mobilization, (ii) O&M Services, (iii) Operator Recruitment and Staffing Plan, (iv) Decommissioning, and (v) Demobilization. On **June 10, 2022**, the Partnership Committee selected the Operator as the preferred proponent with a notification sent to that effect.

[1] The procurement process was made pursuant to the Public-Private Partnership Authority Act (Act 29-2009), the *Regulation for the Procurement, Evaluation, Selection, Negotiation and Award of Public-Private Partnership Contracts Under Act No. 29 Of June 8, 2009*, the Puerto Rico Electric System Transformation Act (Act 120-2018), and the *Regulation for the Procurement, Evaluation, Selection, Negotiation and Award of Partnership Contracts and Sale Contracts for the Transformation of the Electric System under Act No. 120-2018*.

The Proposed Contract complies with the principles set forth in Section 204(b)(2) of PROMESA, to the extent it promotes market competition by stemming from a competitive procurement process. Further, as detailed below, the Proposed Contract is also consistent with PREPA's Certified Fiscal Plan (the "Fiscal Plan"), which requires the transition of the operation and maintenance of PREPA's Puerto Rico base-load generation plants and combustion turbine peaking units (the "Legacy Generation Assets") to a private operator while "leveraging private sector management, experience, and expertise to effectively deliver reliable electricity to Puerto Rico."

The Proposed Contract contemplates operation and maintenance services for the Legacy Generation Assets. In general, the Operator shall:

(i) provide management, operation, maintenance, repair, restoration, replacement and other related services for the Legacy Generation Assets;
(ii) coordinate with the management and maintenance of PREPA Legacy Generation Assets;
(iii) ensure an orderly transfer of the care, custody, and control of the Legacy Generation Assets to Operator without disruption of business continuity;
(iv) prepare written programs that ensure all personnel involved in providing services have the required knowledge, training and experience for their respective assigned duties;
(v) establish a procurement manual;
(vi) procure and supply fuel and other consumables for Legacy Generation Assets;
(vii) propose and execute capital improvements;
(viii) prepare a Communications Plan to ensure that communications with the Government, public officials, regulators, local municipalities and counties, employees, the media, the general public, and others, is timely, effective, efficient and consistent;
(ix) establish an Invoice Review and Approval Procedures Manual;
(x) create Fuel Optimization Plan with savings initiatives, to be approved by the P3A and the Puerto Rico Energy Bureau ("PREB");
(xi) develop a Federally Funded Generation Project Plan, listing and describing those Legacy Generation Asset projects to prioritize in the receipt of federal funding; and
(xii) decommission Legacy Generation Assets when all or a portion of the Legacy Generation Assets cannot continue to be safely operated and maintained.

The Proposed Contract aims to comply with a key pillar and initiative of the Fiscal Plan, the broader PREPA reorganization and the overarching power sector reform (*see* Chapter 10 of the Commonwealth Certified Fiscal Plan). In accordance with the Fiscal Plan, the Proposed Contract has the objectives of boosting generation efficiency, productivity, and environmental compliance, reliability of services, the quality of the supply of electricity, and adherence to environmental and sustainability standards as well as achieving fuel and operational cost savings.

Historically, the Legacy Generation Assets have experienced above industry average forced outage rates primarily due to the average unit age of more than 40 years, which causes generating units to be susceptible to forced outage events that require load shedding.[2] As such, 30% to 40% of PREPA's generation capacity is typically out of service due to units that are indefinitely out of service and in need of significant overhaul. This, combined with PREPA's frequent generating unit outages, makes it necessary to dispatch generation units with higher cost fuel with high frequency, adding to PREPA's ongoing operational costs, as well as resulting in higher customer electricity rates.

PREPA has also historically exceeded planned outage schedule duration by 20% and most units have double-digit annual forced outage rates at two to five times the industry average.[3] Damages resulting from Hurricane Fiona have only worsened existing maintenance issues.[4]

PREPA's aging, inefficient, and unreliable generation fleet must be replaced and modernized. The roadmap for this modernization is defined in the Integrated Resource Plan approved by PREB, which outlines the actions and investment in new generation that must be taken to reduce generation costs and achieve greater reliability and resiliency.[5] Moreover, the Fiscal Plan provides that "[t]o achieve Puerto Rico's energy system transformation, a change in PREPA's historical roles and responsibilities and their reassignment through multiple entities is imperative." Specifically, the Fiscal Plan requires that PREPA's vertically integrated operations must be disaggregated into Generation and T&D utility functions – GenCo and GridCo, respectively.[6]

The professional operation of PREPA's T&D and generation assets forms a critical part of the transformation and the implementation of system modernization, generation upgrades, reliability, efficiency, federal funding, and capital delivery initiatives. The overall objectives of the various private operators are to address and correct many of the operational and infrastructure deficiencies that have plagued PREPA's T&D and generation services over the last decades, improve service quality, and deliver safe, reliable service at affordable rates, as determined by PREB within its rate-setting authority.[7]

Puerto Rico's energy sector transformation rests partly on the opportunity granted via the Proposed Contract to allow a private operator to assume the operation and maintenance of existing Legacy Generation Assets, environmental compliance, safety, and plant retirement and decommissioning, as required by the Fiscal Plan. Notably, the Fiscal Plan also requires the private operator to be

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[2] The condition and performance of PREPA's aging plants has continued to deteriorate availability of the system's generating units dropped by 17% from 2015 to 2020 and has consistently performed below peers. Forced outages of generating units have also seen an increase of 15% over the same period and underperformed peer units, exemplifying the unreliability of PREPA's legacy generating fleet. The net heat rate of generating units has also seen an increase of 377 Btu/kWh from 2016 to 2020. These trends point to growing inefficiencies and unreliability as these units continue to age. The underlying root cause for outages in PREPA's legacy generation plants is related to their age and the need for a well-developed and effectively executed (preventive and pro-active) maintenance program.
[3] *See* LUMA Resource Adequacy Study as filed before the Puerto Rico Energy Bureau on August 30, 2022. Docket Number: NEPR-MI-2022-0002.
[4] *See* Third Update on Stabilization Plan for Temporary Emergency Generation Capacity filed with the Puerto Rico Energy Bureau on December 1, 2022. Docket Number NEPR-MI-2022-0003.
[5] *See* Fiscal Plan at 28-31.
[6] GenCo is comprised of existing PREPA-owned generation resources that are to be operated and maintained by one or more private operators until their retirement, as mandated by Act 17-2019 and outlined in the PREB approved Integrated Resource Plan. *See* Fiscal Plan at 48.
[7] *See* Fiscal Plan at 49.

responsible for working to ensure appropriate short-, mid-, and long-term system planning and timely and efficient execution of system-wide capital improvements.

The Proposed Contract details processes for the procurement and installation of capital spare parts and the implementation of capital improvements across Legacy Generation Assets. Further, pursuant to the Proposed Contract, the T&D Operator shall (i) coordinate the dispatch of power and electricity from available Legacy Generation Assets to the respective interconnection point and provide related services; (ii) coordinate the scheduling of load requirements with the T&D Operator; (iii) develop inputs to T&D Operator with respect to scheduling requirements and capacity requirements taking into consideration unit outages, including, but not limited to, maintenance of program outages, and other operational constraints; (iv) provide information with respect to operational constraints, including air permit constraints; and (v) provide any other related ancillary services.

Pursuant to the Proposed Contract, the P3A and PREPA (through the oversight of the Operator's reporting and deliverables) will ensure compliance with the foregoing Fiscal Plan initiatives, in furtherance of achieving the effective modernization of Puerto Rico's energy sector. Further, the Proposed Contract's performance metrics and incentive/penalty structure will serve to promote the adequate implementation of these requirements.

The Proposed Contract also complies with other adjacent objectives, which will result in benefits to PREPA and its stakeholders. Specifically, the Proposed Contract:

(i) specifically requires compliance with the State Implementation Plan ("SIP") under the definition of "Environmental Law" to make clear that the Operator must comply with the SIP or face penalties for Environmental Noncompliance;

(ii) requires the Operator to offer employment to all full-time PREPA plant Employees who are employed and in good standing as of June 30, 2022. With respect to all other PREPA employees, the Operator must give hiring priority to any PREPA Employee who meets the Operator's employee requirements over other equally qualified applicants for the same job category;

(iii) provides that, as a condition precedent to the Service Commencement Date, the Operator must have executed the joiner agreement to the PREPA Genco-Hydroco Operating Agreement and agreed to the System Operation Principles and the Agreed Operating Procedures attached thereto.[8]

This will provide significant benefits in the coordination of the management and maintenance of PREPA Legacy Generation Assets, as well as facilitate the response to generation related outages, among other things.

The Proposed Contract has a target service commencement date of 14 weeks from the Notice to Proceed. Regarding costs, the Proposed Contract has a Mobilization Fee cap of **$15,000,000** (to

[8] This Operating Agreement involves PREPA, PREPA Genco LLC, PREPA Hydroco LLC, LUMA Energy ServCo LLC, and the P3A and sets out the obligations of these parties with regards to certain matters pertaining to Legacy Generation Assets and Hydropower Assets (as managed by Hydroco).

cover the cost of Mobilization Services); an Annual Service Fee of **$22,500,000**; and Incentive payments (strictly based on its performance of O&M services and Decommissioning Service) capped at **$100,000,000** per year,[9] with O&M and fuel savings arising from the Operator's Fuel Optimization Plan being shared between the Operator and PREPA in equal proportion. Regarding the Incentive Payments, we note that the $100,000,000 cap refers to the maximum share of incentives the Operator could receive in any given year, since it is entitled to receive 50% of all achieved savings. Therefore, in order for the Operator to reach the $100,000,000 cap, it would have had to deliver to PREPA $200,000,000 in total savings, of which half would go to PREPA. Further, if the cap is reached, then any savings in excess of that cap are completely allocated to PREPA.[10]

According to the P3A, PREPA's Budget will be revised to reflect the corresponding allotments to be reprogrammed for payments of the Mobilization Fee under the Proposed Contract. Once service commencement is achieved, Operator payments shall be addressed as part of PREPA's future budgets. As such, the FOMB's review indicates that, upon approval of such reapportionments, PREPA shall have sufficient budgeted funds to cover the cost of the Proposed Contract. Once funds have been allocated in the corresponding accounts, PREPA must submit a Fund Availability Certification in the format included in Appendix A of the FOMB's Contract Submission Questionnaire.

Insofar as the Proposed Contract will be funded with future certified budgets, PREPA must ensure that such budgets incorporate all costs related to the Proposed Contract.

The P3A is expected to inform the FOMB of any budgetary differences other than those specified in Appendix A (Contract Submission Questionnaire) and to request a re-review of the Proposed Contract should any changes occur.

This review was conducted on the basis of information submitted by the P3A. The FOMB has not independently verified the information included in the submission. Should the FOMB become aware of any inaccuracies or misrepresentations – whether intentional or not – it would re-evaluate its assessment.

[9] These incentive payments shall be largely based upon previously non-existent savings. Further, the Operator shall be eligible to receive Incentive Payments strictly based on its performance of O&M services and Decommissioning Services. Certain categories of Incentives and Penalties include minimum standards of performance that the Operator must meet; with failure to meet such standards possibly resulting in a "Minimum Performance Threshold Default," as defined therein. The Operator shall be evaluated on the following categories (i) Operation Cost Efficiency; (ii) Equivalent Availability Factor; (iii) Safety Compliance; (iv) Environmental Compliance; (v) Reporting Obligations; and (vi) Fuel Savings.

[10] For example, if the Operator achieves $250 million in savings in a year, it would receive $100 million of those savings, and PREPA would receive $150 million.