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How Can Caribbean Countries Make the Transition to Regulated Electricity Markets? Case Study: Puerto Rico

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The Regulatory Assistance Project (RAP)

We are a global, non-profit team of experts focused on the long-term economic and environmental sustainability of the power and natural gas sectors, providing assistance to government officials on a broad range of energy and environmental issues.

About RAP – US

RAP provides technical and policy support at the federal, state, and regional levels, advising utility and air regulators and their staff, legislators, governors, other officials, and national organizations.

We help states achieve ambitious energy efficiency and renewable energy targets and we provide tailored analysis and recommendations on topics such as ratemaking, smart grid, decoupling, and clean energy resources. RAP publishes papers on emerging regulatory issues, and we conduct state-by-state research that tracks policy implementation.

Background

- Puerto Rico had one government-owned unregulated utility, the Puerto Rican Electric Power Authority (PREPA) that did its own resource planning and set rates. (Lack of transparency and public accountability)
- The average electric rate is \$.27
- There is an aged fleet of inefficient generation that is dependent on expensive, foreign-sourced, and volatily priced fossil fuels (largely oil)
- Fragile financials made bondholder concerns a central focus (PREPA is undergoing financial restructuring with a new chief officer of restructuring).
- Many local governments had highly subsidized rates and were inefficient in their use of electricity

Regulatory Assistance Project Report

- RAP prepared a report for the Center for a New Economy in Puerto Rico entitled: *The Role of a Power Sector Regulator to Strengthen Sector Performance in Puerto Rico*.
- The paper makes a number of recommendations for establishing a robust and independent regulator.
- The paper can be found on RAP's website:
<http://www.raonline.org/document/download/id/7043>

Key Characteristics of a Good Regulatory Authority

- **Establish Clear Roles and Responsibilities, and Legislative Intent** – The roles and responsibilities, along with legislative intent for the Commission should be clearly spelled out in legislation.
- **Establish Necessary Authority and Tools** – The Commission should have clear authority and the requisite tools to perform its duties in accordance with the legislative intent.
- **Ensure that the Institution is Comprised of Commissioner-Level Experts with Integrity** – Appointments should be based on merit and integrity rather than political affiliation.
- **Ensure Adequate Accountability** – The Commission should be held to the responsibility of fulfilling its mission with the filing of annual reports to the legislature, and through the legislative hearings, among other requirements to earn the public trust. Accountability also includes adherence to the highest ethical standards.

Key Characteristics of a Good Regulatory Authority

- **Establish High Standards of Fair, Transparent, and Efficient Processes** – The regulator should establish procedures that set high standards for fair, transparent, and efficient process.
- **Establish Adequate Funding and Ensure it is Empowered with Adequate Staff and Technical Support** – The Commission should be adequately staffed and funded to deliver on its mission. The funding of the Commission should be sourced to services from the electricity sector, ideally based on gross revenues generated in Puerto Rico or volume of sales.
- **Promote Sound Long-Range, Least-Cost Planning** – The planning framework should broadly frame objectives around minimizing costs through a portfolio of solutions that carefully compare and test a range of options. This is most effectively captured through a robust integrated resource planning (IRP) framework.

Key Characteristics of a Good Regulatory Authority

- **Promote Energy Efficiency and Customer-Sided Resources** – Strong consideration of alternative sources of energy can help build energy independence in Puerto Rico, which is important given the cost of importing fuel.
- **Promote High Standards of Service Quality, Reliability, and Consumer Protection** – The regulator should promote high standards of service quality, system reliability, and basic consumer protections.
- **Ensure an Effective Consumer Advocate Voice** – The regulator should have the benefit of more than one expert voice and perspective in the hearing room. The legislature should establish a separate consumer advocate with resources adequate to the task.

So What Needs to Happen?

- Pass legislation to create a Regulatory Authority
- Include the adoption of a consumer advocate office as discussed in the RAP paper below:

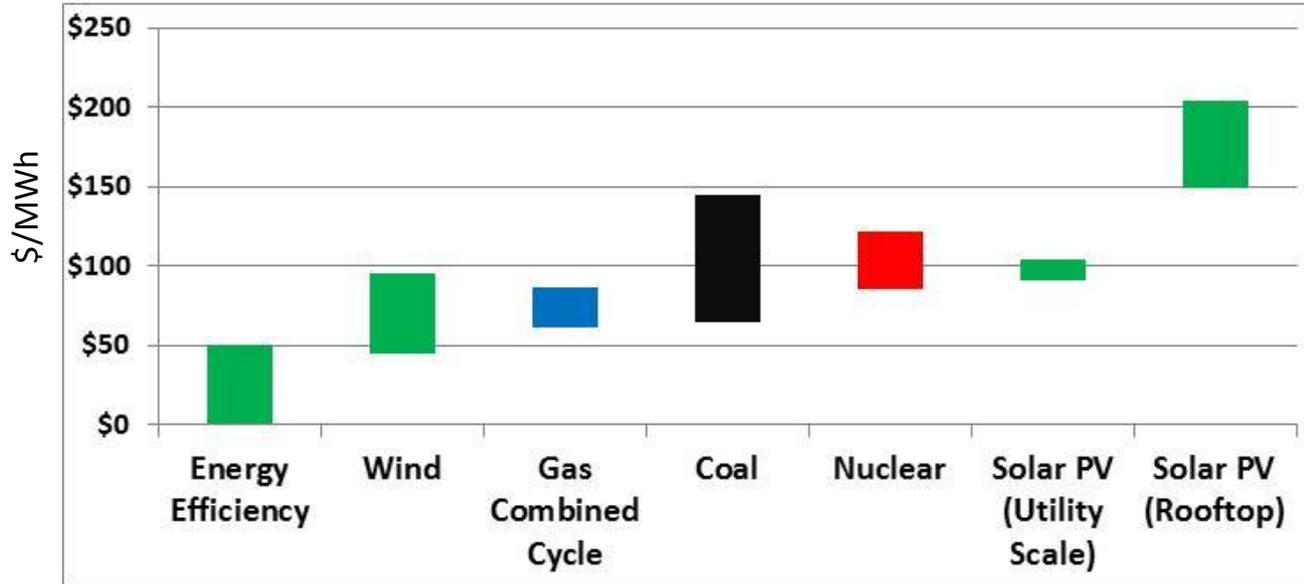
<http://www.raonline.org/document/download/id/7106>

Resource Planning is an Important Element

Conduct planning review to determine:

- Which plants are operating efficiently?
- Which plants should be retired?
- What are the fuel costs associated with the plants?
- Which plants are owned by the utility?
- How much energy is provided through a Purchased Power Contract and what is the term?
- Are there lesser cost options such as energy efficiency, demand response, distributed generation?
- What is the anticipated growth in demand over the planning horizon?

General Cost of Resource Options



Source: Lazard, 2014

Full Review/Audit of Utility

An audit can create the baseline and identify cost savings that can lower rates by analyzing the following:

- Inefficiencies in management and expenditures
- Subsidies that raise rates for other customers
- Reductions in expenses – are services and supplies competitively bid to get the best price?
- Customer service issues – handling of complaints, collections
- Reliability issues – no revenues generated from power outage

Highlights of Puerto Rico's Legislation SB 837

Creation of a Regulatory Commission

- 3 Commissioners appointed by the Governor with advice and consent of Senate
- Commissioners must be a lawyer or have a masters or doctorate in engineering, finance, economics or related field, with 5 years' experience in energy matters and 10 years' experience in their profession.
- **Ethical requirements to ensure independence and no conflict of interest, including 2 year revolving door requirement – (Independence, transparency and ethics are stressed throughout the legislation)**
- During first six years one of the three shall have experience as a commissioner
- Staggered terms of 6 years
- 3 public meetings per month

Major Duties of the Commission

- Overseeing implementation of energy policy and rules to carry out the objectives
- Formulate and implement strategies to permanently reduce and stabilize energy costs
- Approve or modify short, medium and long-term plans for IRP
- Develop and implement standards of EE and conservation
- Review, revise and approve rates
- Certify suppliers
- Monitor compliance with any RPS

Major Duties of the Commission

- Review and approve minimum technical requirements for Interconnection
- Establish reliability standards
- Inspect and perform audits on all types of records, inventories, documents and physical facilities of PREPA and any other company of energy company Carry out studies and research on a broad array of issues
- Create public webpage to access information
- Ensure regulation communication with FERC, EPA and other federal agencies
- Issue citations and penalties
- Submit annual reports to Legislature
- Review consumer complaints

Creation of a Consumer Advocacy Agency

- Purpose is to educate, guide, attend and represent customers
- The Office will be sponsored by and will have their operational base in the Commission and receive from the AEPR, administrative support
- ICPO will work as an independent body of the Commission, of the State Office of public energy policy, of the authority and any energy company certified in the Commonwealth of Puerto Rico.
- Executive Director
 - The Director shall be appointed by the Governor with the advice and consent of the Senate for a term of six years
 - Must be licensed attorney with minimum of 5 years of experience

Regulation of PREPA

- Allows the legislature to obtain detailed information pertaining to the finances, operations and costs.
- Creates a 9 member Governing Board of which two represent residential interests and one represents business; others must have various technical expertise. Combination of appointed and elected membership.
- Strict prohibitions against conflict of interest for Board.
- Board hires executive director of PREPA as well as an Auditor-General who reports findings directly to the Board.
- Board meetings transmitted in real time on internet and posted for later viewing.
- All PREPA contracts posted on the internet.
- Board holds an annual public meeting.
- Role of Board is to provide strategic direction for Executive Director to execute.
- Creates a three-member audit committee.

Other Provisions of SB 837

- Creation of an Energy Office responsible for energy planning
- Creates an independent autonomous body providing administrative and operational support to Commission, Energy Office and Consumer Advocate office
- Creation of Integrated Resource Plan and requirement that PREPA file a 20 year plan within 2 years with stakeholder input.
- Creation of a 2% stabilization fund to be used for energy efficiency, renewable energy and grid infrastructure
- Requirements for municipalities to reduce energy consumption by 5%/year over next 3 years with penalties for noncompliance – municipalities will be required to pay for energy – reducing subsidy

Other Provisions of SB 837

- Informational filing requirements for all certified electric power suppliers
- Energy savings requirements for all branches of government
- Complaint process for consumers
- Informational filing requirements for all certified electric power suppliers
- Requirement that at least 60% of fossil fuel fleet is “highly efficient”

Other Provisions of SB 837

- Net-metering interconnection requirements and customer education
- Establishment by Commission of competitive bidding process for generation
- Commission approval for expansion and construction of new facilities
- Commission approval for transfers, mergers and acquisitions
- Commission authority to impose penalties for non compliance
- Appeals process

Status To Date

- Note that SB 837 took approximately six months to draft and pass with input from multiple stakeholders.
- Puerto Rico is focused on the restructuring and ensuring that PREPA can make its bond payments
- Two commissioners have been appointed by the Governor and are going through the Senate confirmation process
- PREPA is supposed to release the first installment of funds for the Commission's budget this week

Conclusion

- Creation of a regulatory entity is doable – lots of work ahead for Puerto Rico
- Legislation needs to be comprehensive in scope to address rates and the underlying causes for high rates
- Need to provide regulator with the authority necessary to carry out public interest
- Smaller islands may consider pooling resources for a regional commission – not unlike state Regional Transmission Organizations that operate the utility transmission system over multiple states
- A Commission oversight board with representatives of each nation to set policy direction for Commission to implement could be a model

About RAP

The Regulatory Assistance Project (RAP) is a global, non-profit team of experts that focuses on the long-term economic and environmental sustainability of the power and natural gas sectors. RAP has deep expertise in regulatory and market policies that:

- Promote economic efficiency
- Protect the environment
- Ensure system reliability
- Allocate system benefits fairly among all consumers

Learn more about RAP at www.raponline.org

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