

August 11, 2021

VIA EMAIL AND HAND DELIVERY

Mr. Ralph A. Kreil-Rivera – President
The Governing Board of the Puerto Rico Electric Power Authority

Members of the Governing Board of the Puerto Rico Electric Power Authority

Mr. Efrán Paredes-Maisonet - Executive Director
Puerto Rico Electric Power Authority
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Re: Notice of Challenges Threatening AES Puerto Rico, L.P.'s Continued Operations

Dear Mr. Ralph A. Kreil-Rivera, Members of the Governing Board and Mr. Paredes-Maisonet:

On behalf of AES Puerto Rico, L.P. (AES-PR), I wanted to update the Puerto Rico Electric Power Authority (PREPA) on the serious challenges that we continue to face and that may impair our ability to operate successfully and to continue to provide highly reliable, low-cost, baseload electricity under our Power Purchase and Operating Agreement (PPOA) with PREPA. These challenges can be mitigated if both AES-PR and PREPA collaborate in transitioning AES-PR's coal-fueled power plant in Guayama into a renewable power source. This effort should be undertaken swiftly given the significant risks outlined below.

As you know, AES-PR supports responsible efforts to accelerate the island's transition to renewable power generation through retirement of our coal-fueled power plant in Guayama from baseload operations before 2027. As we outlined previously for PREPA and other Commonwealth and federal officials, AES-PR would replace the energy from our coal-fueled power plant with state-of-the-art solar facilities with battery storage. The new facilities would include the Maverick 5B technology which uses 50% less land than a traditional solar project and can be built three times faster than other solar resources. The electricity price charged by these facilities would be similar to what we are currently charging under our PPOA.

We appreciate PREPA's desire to retain the reliable baseload power that our coal-fueled power plant has provided through the end of our current PPOA. We at AES-PR understand the importance of reliable energy. However, what we are proposing is a resilient and proven technology, able to withstand major hurricanes, that can be transitioned into place. As the

renewable resources come online, electricity produced from coal would be systematically reduced, while the current plant would remain available to ensure grid reliability during emergencies.

This transition can be achieved by working together with PREPA and the Government of Puerto Rico to enter into an agreement that is in accordance with the existing contractual rights and responsibilities under the current PPOA. Indeed, in Puerto Rico Law 17-2019, the Puerto Rico legislature streamlined the permitting process for a new generating source to replace our coal-fueled capacity, thereby demonstrating its intention to encourage the parties to work together and providing PREPA the confidence that the new resource can be brought swiftly online. Thus, once an agreement is reached, a transition to renewable energy resources could be completed in less than two years. To facilitate this, AES-PR would draw on AES' global experience in renewable energy transitions, as AES understands the importance of proper planning to ensure that reliable energy is available during these transitions.

That is why we proposed in our June 28, 2021 Memorandum of Understanding (copy enclosed) to PREPA that AES-PR transfer ownership of its coal-fueled units in order to focus on constructing renewable sources (that is, wind, solar, and/or energy storage) that would provide Puerto Rico with 280-500 MW of reliable electricity for a period of 25 years or longer. AES-PR is well-positioned to implement this plan, under which (1) PREPA or the appropriate Puerto Rico governmental entity would take over from AES-PR ownership of the plant, while (2) AES-PR would contract to continue to operate and maintain the coal-fueled power plant to ensure it provides PREPA and the people of Puerto Rico the necessary reserve capacity.¹ In our view, this proposal would secure Puerto Rico's energy supply, protect the environment, and eliminate the ongoing challenges that threaten AES-PR's ability to operate.

Unfortunately, we must be absolutely clear: Unless PREPA makes a concerted effort to transition the role of our coal-fueled plant on the grid, there is a real risk that AES-PR may not be able to continue to meet the challenges threatening its continued operations in the near future, let alone through 2027. Accordingly, AES-PR must put PREPA on notice of these challenges and of how tenuous our ability is to operate.

Challenges Threatening AES-PR's Continued Operations

As we outlined for you in our March 24, 2021 letter (copy enclosed), AES-PR's cashflow situation has deteriorated significantly, and continues to worsen, due to over \$186 million in new operational costs imposed on AES-PR as a result of unforeseen regulatory and logistical challenges.

- **Environmental costs.** We continue to face greatly increased environmental costs due to Puerto Rico's Act 5-2020, the unprecedented ban on disposal in Puerto Rico of the coal combustion residuals ("CCRs") we produce when we generate electricity for the citizens of Puerto Rico. No other state in the nation has a similar ban. Puerto Rico has multiple state-of-the-art landfills that meet the rigorous requirements established by Subtitle D of the federal Resource Conservation and Recovery Act (RCRA)—including an engineered impermeable liner, daily cover, leachate collection and groundwater monitoring to ensure

¹ See the June 28, 2021 Memorandum of Understanding for further details on this proposal.

secure and safe disposal—and that are permitted to receive our CCR. Nonetheless, instead of using the qualified landfills here on the island that are located an hour’s drive from our coal-fueled power plant, Puerto Rico’s new law has required us to rely on a 1000-mile+ delivery chain to barge CCRs to the continental United States, where the CCRs must then be transferred to trucks for further delivery to a qualified landfill. That will impose at least \$167 million in additional costs on AES-PR through 2027.

- Port maintenance costs. We also have incurred and will incur additional costs if required to undertake essential maintenance (dredging) at the Port of Las Mareas. Under the Marine Facilities Agreement (“MFA”) between AES-PR and the Puerto Rico Ports Authority (the “Authority”), the Authority is responsible for all dredging and cleaning of the Port. However, in clear breach of the MFA, the Authority has not met its responsibility, leaving AES-PR to bear \$7.8 million in additional expenses to date – with another \$8 million expected through 2027.
- EAF penalties. At PREPA’s request, AES-PR delayed scheduled maintenance and stayed online to serve customer demand when other PREPA assets could not meet load due to damages caused by earthquakes. As well as causing additional stress on our facility, which could lead to accelerated deterioration or even failure of our equipment, the delayed maintenance has affected AES-PR’s Equivalent Availability Factor (EAF). That could result in EAF penalties under the PPOA of \$11.4 million, which would further exacerbate AES-PR’s cash flow challenges.

To date, AES-PR has met these additional burdens and continued to provide reliable, resilient, and low-cost power. We have done so when other resources were not available to PREPA—such as after Hurricane Maria or the earthquakes last year. With these ever-increasing costs, the AES-PR cashflow situation has worsened leaving it in an increasingly dire situation.

However, this already tenuous situation has become even more fragile. As you know, Puerto Rico’s ban on CCR disposal also precludes AES-PR from holding CCR at our facility more than 180 days, before we must remove it from our facility. Recently, Puerto Rico’s Department of Environmental Resources (DNER) issued rules that further restricted the 180-days requirement, mandating that CCR stored temporarily at our facility must eventually be placed on a lined area. According to the statute, failure to comply with Act 5 would be a criminal violation, subject to fines and imprisonment.

Under no circumstances will AES-PR put its personnel or our company at risk of criminal charges. Thus, the actions of Puerto Rico, namely, Act 5 and the DNER implementing rules, have created a problem whereby any disruption along the lengthy delivery chain to the continental U.S. could leave AES-PR unable to operate. For one, to comply with the law, we must reduce the volume of CCR onsite to create sufficient open space to place the new liner, which we intend to do in two phases. To reduce the volume, however, depends on our ability to timely move CCR offsite through our delivery chain to the U.S. If the chain is disrupted and we cannot move our CCR, then we cannot place the liner and the law could leave AES-PR unable to operate.

Moreover, even assuming we can place the liner successfully, the 180-day restriction likewise means we must have consistent access to barges and a disposal site in the continental U.S. However, as we advised PREPA previously, despite substantial efforts, our reliable disposal

options are extremely limited. See AES-PR's June 3, 2019 Letter to PREPA (J. Ortiz) (copy enclosed). At present, we have only a single disposal site available to us. Thus, if we do not have access to enough barges or if the sole disposal site is unavailable for any reason, the restrictions imposed by Puerto Rico law under Act 5 and the DNER rules may prevent AES-PR from being able to operate.

The only delivery chain left to AES-PR relies on extremely fragile logistics. As outlined previously, AES-PR has retained the services of Moran Transportation, a 160-year-old US-based shipping company that is a respected provider of bulk marine transportation services, to barge our CCR 1000+ miles away to a Florida port, from which we arrange for delivery by trucks to a subtitle D landfill in Georgia. AES-PR's options to send the material by barge are extraordinarily limited, as federal law requires the barges to comply with the Jones Act. This leaves us with quite literally only a handful of Jones Act-qualified barges that serve Puerto Rico. If just one barge is unavailable, the fragile delivery chain can be disrupted if not broken entirely.

Indeed, earlier this year, the *Bridgeport*, a Moran barge carrying material from AES-PR foundered off the coast of Jacksonville—a maritime incident for which AES-PR bears no responsibility as the charterer of the vessel. That barge has only recently been refloated and will need to be repaired. That has left AES-PR without access to one of the largest Moran barges to remove CCR, and its future availability will depend upon if and when repairs on the *Bridgeport* can be completed successfully. The resumed shipping operations of the *Bridgeport* is crucial: Our schedule to complete installation of the mandatory liner depends upon Moran being able to return the barge to service this fall.

Moreover, during the incident, the *Bridgeport* released some of its CCR cargo into the St. John's River. Moran and its agents have been responding to the incident and working with regulators, including the Florida Department of Environmental Protection. We believe there has been no resulting harm to human health or the environment from the release. However, there has been considerable media, political, and public interest in the incident. If there are future restrictions on moving CCR through the Jacksonville port, that could also disrupt AES-PR's fragile delivery chain.

Access to landfills in the continental U.S. is likewise extremely fragile, as opposition to our coal-fueled plant has extended to our lawful use or disposal of CCR outside of Puerto Rico. As we explained, the on-island opponents of our plant joined with local activists to protest the delivery of our CCRs to a lined, subtitle D landfill in Florida. AES-PR June 3, 2019 Letter at 2. As a result, the county board pressed the landfill operator to stop taking any more CCRs from AES-PR and the landfill agreed. We were able to enter into a new contract with a qualified landfill in Georgia, but that remains the only disposal site that has agreed to take our material. Opposition similar to that in Florida could disrupt critical deliveries of our CCR to the continental United States – if not freeze us entirely out of disposal options in the U.S.

In addition to these extraordinary supply chain challenges, Puerto Rico DNER has recently finalized additional new CCR regulations. These new regulations go substantially beyond the requirements that EPA has imposed on AES-PR under the federal CCR Rule. Over the past six years AES-PR has complied fully with the federal CCR requirements. After multiple rounds of groundwater monitoring under the rigorous program established by the federal rule, and after

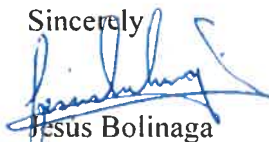
considering public input, AES-PR is now installing a liner (as noted) that will address potential concerns regarding the CCR temporarily stored at our facility. Now, under the new DNER regulations, AES-PR will have to conduct more groundwater monitoring for an expanded set of parameters with additional groundwater protection standards and possibly requiring an increased number of well locations at our facility. Depending on the results, additional costly corrective measures may have to be considered beyond those already being implemented at substantial expense under the federal CCR Rule. Moreover, the rules authorize DNER to approve any corrective measures selected under the Puerto Rico rules, which may mean corrective measures demanded by a government authority will impose significant additional and untenable financial burdens on our ability to provide reliable, low-cost electricity as we have over the past two decades.

We bring these matters to your attention to reiterate for you both the financial and logistical challenges AES-PR is facing in its efforts to sustain reliable operations in Puerto Rico. Resolving the cashflow shortfall is crucial to AES-PR's ability to provide reliable, uninterrupted power. Moreover, as the cashflow shortfall leaves us with absolutely no cushion to deal with contingencies, including logistical problems that would arise in managing our CCR if the legal restrictions imposed by the Puerto Rico government disrupt our fragile CCR delivery chain. If these contingencies materialize, we will have no choice but to exercise our legal rights, including to assert force majeure under Article 17 of the PPOA. However, as noted above, this risk can be avoided if we and PREPA act quickly to responsibly transition PREPA's reliance on energy from our coal-fueled plant to a renewable power source.

Finally, as we advised previously, because AES-PR provides 25% of the electricity used the island, PREPA should have contingencies in place if AES-PR is prevented from operating, so that PREPA can ensure the reliable delivery of power on the island. *See* AES-PR's June 3, 2019 Letter to PREPA (J. Ortiz).

We would appreciate your comments on these issues and concrete recommendations on how to work together going forward.

Sincerely



Jesus Bolinaga
President

AES Puerto Rico, L.P.

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