

The \$586 million mystery

Recently, the Center for the New Economy, a non-profit, non-partisan think tank where I work, published a study analyzing the state of the Puerto Rico electricity sector.

Among other things, the study found that the Puerto Rico Electric Power Authority, which operates as a vertically-integrated, self-regulated monopoly with the market power and legal authority to recover its costs from its customers, reported a net loss of \$24 million for the fiscal year ended June 30, 2004.

PREPA has publicly admitted this loss but instead of explaining it and offering a full accounting to the people of Puerto Rico, who in the final analysis are its shareholders, it has arrogantly tried to dismiss it as insignificant in a corporation with annual revenues in excess of \$2.5 billion.

In our view, the fact that PREPA, a monopoly, reported a financial loss, even if it were only in the amount of \$1, is indicative of the existence of severe managerial and operating deficiencies which should be addressed as soon as possible because without access to relatively affordable and reliable electric power it will be extremely difficult, if not outright impossible, to promote sustained growth in basically any area of economic endeavor in Puerto Rico in the near future.

The study also found that PREPA has overcharged its clients by billing them for payments that as a matter of public policy it is required to make in lieu of taxes. According to our analysis, PREPA overcharged its clients by an amount in excess of \$586 million between June 2000 and June 2004. To add insult to injury, due to contractual restrictions, PREPA was not permitted to pay in full the amounts it was otherwise required to pay in lieu of taxes during that five-year period. Yet, PREPA "recovered" from its clients the full amount it was obligated to pay in lieu of taxes instead of the lower amount it actually paid.

PREPA claims that it is legally obligated to charge its clients for these payments in lieu of taxes. However, even a cursory examination of the formula that was in effect during the period between June 2000 and June 2004 reveals that this is simply not true. The law required PREPA to retain from its net income an amount equal to 11 percent of its gross income for purposes of making these payments. Nowhere in the law is there an obligation requiring PREPA to invoice its customers for these amounts, just as there is no legal requirement to hide these amounts in the fuel and purchased power charges.

It could be argued that all businesses try to pass on to their customers costs associated with operating inefficiencies and with taxes. PREPA, however, is not like any other business. It is a publicly-chartered monopoly, created for the purpose of promoting the eco-



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conomic development of Puerto Rico. As such, it is not subject to competition and other market pressures that would limit its ability to pass on these costs to its customers. Second, PREPA is required to make payments in lieu of taxes because the Puerto Rico Legislature decided as a matter of public policy that PREPA should make these payments. There is no reasonable argument to justify the recovery of these payments as long as PREPA remains a government-owned corporation.

Furthermore, PREPA's obligation to make these payments is completely unrelated to its fuel and purchased power requirements. There is no valid reason, other than obfuscating and concealing the truth, to sneak-in the recovery of these payments into the formulae for calculating the fuel and purchased power charges. In the name of transparency, the recovery of these contributions in lieu of taxes, if it is allowed to take place at all, should be separate and independent from the recovery of fuel and purchased power costs. Finally, PREPA has not made these payments in full during the past five years, yet it has charged its customers for the full amount.

Given this situation, Gov. Acevedo Vilá should take the lead and submit legislation to prohibit PREPA from recovering these payments in lieu of taxes. An immediate reduction of 11 percent in the average electricity invoice would be a great relief to the working people of Puerto Rico at a time when the prices for many basic goods and services are expected to increase. It would also remind the bureaucratic Brahmins at PREPA that their primary mission is to serve the interests of the people of Puerto Rico and not the interests of bondholders, suppliers or political parties.

You can download the PREPA study free of charge from CNE's Website at www.grupocne.org.

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