



# DEFINITIVE PROPOSAL FORM 1.3

## CONFIRMATION OF ACCEPTANCE OF O&M AGREEMENT

PSEG Puerto Rico LLC (the Qualified Respondent) hereby acknowledges and affirms the following:

1. The Qualified Respondent's Definitive Proposal is based on the final form of the O&M Agreement and the information contained in the Data Room as of the date of the Proposal submission Deadline.
2. The Qualified Respondent accepts and agrees to execute the final form of the O&M Agreement, save for the terms and conditions contemplated for the Qualified Respondent's Definitive Proposal described in Section 4.1.8 (*Operational and Financial Proposals*) of the RFP, immaterial amendments to incorporate party names, details and execution mechanics, and subject to further discussion on the following material comments:

**See attachment A which is incorporated by reference herein.**

Capitalized terms not defined herein shall have the meaning set forth in the Request for Proposals for Puerto Rico Electric Power Transmission and Distribution System issued by the Puerto Rico Public-Private Partnerships Authority on February 1, 2019 (as amended and supplemented, the "RFP") or the final form of the Puerto Rico Transmission and Distribution System Operation and Maintenance Agreement (the "O&M Agreement"). If there is a term defined in both, and their definitions conflict, the definition in the O&M Agreement shall prevail..

PSEG Puerto Rico LLC  
**QUALIFIED RESPONDENT**  
Company Name

Daniel Eichhorn  
Name of Qualified Respondent's  
Authorized Official

President - PSEG Puerto Rico LLC  
Title

  
Signature of Qualified Respondent's  
Authorized Official

November 25, 2019  
Date

### 1.3 Confirmation of Acceptance of O&M Agreement

## Attachment A

### To Definitive Proposal Form 1.3

### Confirmation of Acceptance of O&M Agreement

We appreciate the effort by PREPA and P3 in preparing the OMA and their consideration of our comments to date. In the event that PSEG Puerto Rico LLC (“PSEG”) is selected, PSEG is confident that in the negotiation process contemplated by Section 3.7 of the RFP, the Parties will be able to reach resolution of the remaining issues to each Party’s satisfaction resulting in an OMA that can be executed by the Parties and lead to a long and successful relationship.

The following is a summary of PSEG’s material comments with respect to O&M Agreement which require further negotiation and agreement to the satisfaction of PSEG, PREPA and P3:

1. Adequate FEMA Funding: We note and appreciate the addition of the new Section 4.5(i). However, simply including “adequate funding for Capital Costs for the first three (3) years of the Term” as part of the Initial Budget does not address PSEG’s concerns. As we have repeatedly stated, it is critical that there be adequate funding in order to rebuild and modernize PREPA’s T&D System so that it can operate consistent with industry standards and PSEG can seek to meet/exceed its performance expectations. We had previously requested that the OMA be revised to require that a minimum amount of FEMA funds be obligated and available both at the outset of operations services and then periodically (every third anniversary) during the Term of the OMA. The new Section 4.5(i) appears to be an attempt to address our concerns regarding a minimum level of FEMA funding being available before O&M Services are commenced. To address PSEG’s concern adequately, the OMA should be further revised by (a) moving Section 4.2(e) (Initial Budgets) to either Section 4.1 or Section 4.5 (similar to the recent change to the Shared Services Agreement condition precedent), so that it is clear that finalizing the Initial Budget (including Capital Costs) is no longer a ManagementCo Service Commencement Date Condition that carries the risk of Delay Liquidated Damages, and (b) clarifying in Section 4.5(g) that the Initial Budget, which budget should include obligated and available FEMA funding, approved by PREB must be acceptable to PSEG in its sole discretion in order for the Initial Budget condition precedent to be satisfied. With respect to FEMA funding during the Term of the OMA, Section 7.3 of the OMA should be revised to provide that the Capital Budgets in Contract Year 4 and (every 3 years thereafter) would need to include an amount of obligated and available FEMA funding consistent with the funding requirements in the System Remediation Plan for those years.
  
2. Mutual Agreement As to Initial Budget/Performance Metrics/Vegetation Management Plan:
  - a. The Initial Budget (which we understand will include IRP costs) and Performance Metrics are each a condition precedent to the commencement of O&M Services (Sections 4.5(g) and (h)). We require that the OMA be further revised by (a) moving Sections 4.2(e) (Initial Budgets) and 4.2(f) (Performance Metrics) to either Section 4.1 or Section 4.5 (similar to the recent change to the Shared Services Agreement condition precedent), so that it is clear that finalizing the Initial Budget and Performance Metrics are no longer a ManagementCo Service Commencement Date Condition that carries the risk of Delay Liquidated Damages, and (b) clarifying in Section 4.5(g) and (h) that the Initial Budget and Performance Metrics approved by PREB must be acceptable to PSEG in its sole discretion in order for the Initial Budget and Performance Metrics conditions precedent to be satisfied. We fully recognize the PREB’s authority regarding setting rates and other

regulatory matters and we are not attempting to usurp that authority in any way. We similarly do not want our agreement on the budgets and metrics with the Administrator to be overridden by the PREB and be forced to operate the system without what we believe to be sufficient funding to meet our obligations under the OMA.

- b. The current state of PREPA's vegetation management requires that it receive considerable attention before it can be managed on a more routine basis. We believe that this situation lends itself to the development of a comprehensive vegetation management plan as reflected in the OMA. The plan is a necessary corollary to the System Remediation Plan. PREPA's estimate for this work contained in the Sargent and Lundy report suggests the total costs for this work will be in excess of \$800 million for the T&D System. Our assessment is that Sargent and Lundy's estimate is reasonable. We will be proposing a plan to perform this work over a 4 year period the cost of which will be included in the Initial Budget and thereafter. We believe that such work will meaningfully improve reliability for customers (and increase load) and meaningfully reduce system transmission constraints and reduce instances of uneconomic generation dispatch.
3. Automatic Transfer of Operating Company: We appreciate the addition of the new language in Section 16.3 which serves to highlight PSEG's concerns that it could be left with significant obligations in the event it needs to handle the winding-up of ServCo after the expiry or termination of the OMA (even if terminated by PSEG). As part of providing O&M Services, the Management Company, as required by the OMA, is creating ServCo to provide all of the day-to-day O&M Services. The cost and liabilities associated with ServCo's operations are governed by the OMA and at such time as the OMA expires or terminates PREPA should be responsible for the costs and liabilities of ServCo. While PSEG is prepared to work with PREPA on agreeing to a Back-End Transition Plan that recognizes the concerns of both parties (and any incoming operator) prior to the commencement of the Back-End Transition, the OMA must be revised to provide that ServCo will be automatically transferred to PREPA (or its designee) at the time the OMA expires or the termination date. We understand, P3's expressed concerns that with the automatic transfer of ServCo it could assume liabilities beyond those permitted by the OMA. However, the OMA already has protections for this scenario, including the specific requirement in Section 5.20 (Other Services), that ServCo may not engage in any business or activity other than to employ ServCo employees and to provide O&M Services pursuant to the OMA. If ServCo was used for any other purposes (e.g., raising debt or saddling ServCo with liabilities not already permitted the OMA), PSEG would be in breach of the OMA and PREPA/P3 will be entitled to the protections of the OMA, including recourse against the Guarantor if PSEG did not pay the costs of the breach. There are significant audit and investigation rights that PREPA/P3 can avail itself of during the term which rights would certainly uncover any of the expressed issues of concern before expiration or termination of the OMA.
4. Litigation as a Final Resort: Except for Technical Disputes, any Dispute not resolved through Negotiation shall be submitted to non-binding mediation, should both parties consent to its submission. Thereafter, any disputes not resolved will be resolved through litigation pursuant to Section 15.6 (Litigation as a Final Resort). In this regard, we propose that Section 15.6(a) be modified to require that venue for Disputes, other than Technical Disputes, be initiated in only Delaware state or federal court. In addition, the Administrator Dispute, which involves a claim by the Administrator that the Operator is in default and exercise remedies (Section 6.2 (a)(ix)), should not be considered a Technical Dispute and instead be resolved in accordance with Section 15.6. The venue for the resolution of Technical Disputes should be in a neutral venue such as New York.

5. Capped Payment Guaranty: The guaranty form provided in Exhibit D should be a payment-only guaranty and contain a maximum liability amount. In addition, we do not see a reason (nor is it possible) that the guarantor be incorporated in Puerto Rico as currently provided in the form of guaranty. A performance guaranty in the context of a services arrangement of this type introduces considerable uncertainty as to what would be required of the guarantor. An uncapped guaranty is, moreover, commercially unreasonable and would require that PSEG have unfettered control comparable to that of an owner and a materially higher service fee. PSEG's guaranty will be from an investment grade affiliate of PSEG Puerto Rico LLC, it will contain a meaningful maximum liability amount consistent with its proposed service fee and be in a form routinely used and accepted by counterparties in transactions with PSEG companies.
6. Acceptability of Conditions to Execution of the OMA: The governmental approvals and other items that are conditions to the execution of the OMA in Section 2.2 of the OMA, must be either without condition or modification to the contract, or, if any such changes, be acceptable to PSEG in its sole discretion. It is not reasonable for a party to a contract to be put in a position where a governmental approval imposes conditions, requirements or modifications to such contract that have not been agreed to and are unacceptable to that party, to then be required to either execute the contract or risk forfeiting its bid security.
7. Limitation on Liability:
  - a. The limitation of liability proposed by PREPA in Section 14.6(d)(ii) of the OMA is acceptable so long as bad faith and willful breach of the OMA are additional exceptions and in such cases the damages will not be subject to a cap.
  - b. We request that P3 explain the modification P3 made in the November 15 draft to the limitation on liability in Section 18.3(a)(i) as it appears that this modification may expose PSEG to unlimited liability for certain claims. This, of course, would be contrary to various liability caps in the OMA. Further, Section 18.5 should be clarified that the limitation for consequential damages only applies to claims against each other but not for third party claims covered by the indemnification obligations.
8. Pre-Existing Environmental Conditions/Baseline Environmental Study:
  - a. The definition of "Pre-Existing Environmental Conditions" should be expanded to include all pre-existing non-compliant environmental conditions and not be limited to environmental conditions involving discharges. For example, the improper storage of a transformer containing PCBs ought to be within the definition of what constitutes a Pre-Existing Environmental Condition. This change to the OMA should not be controversial.
  - b. It does not appear from Section 4.5(f) that PSEG has any input into this Study. PSEG should have the opportunity to review and comment on the scope and final report of the Environmental Baseline Study but this should not be deemed to constitute approval by PSEG of the Study.
9. Ability to Terminate Due to Change in Law: PSEG should have a right to either terminate or amend the OMA in the event of a "Change in Law" without having to wait 18 months or 4 months, respectively, as provided in Section 17.2(c) of the OMA. Shortening the period with

respect to an amendment may, in fact, avoid a termination.

10. The OMA and PREB: The regulatory framework should take into account the fact that an entity pursuant to a contract will be operating and maintaining PREPA's T&D System. Actions taken by PREB that are required by the OMA, e.g. rate setting, required approvals under the OMA, or new regulatory requirements/restrictions, must enable PSEG to meet its obligations to provide O&M Services and provide PSEG with a reasonable opportunity to earn the Service Fee in full. This standard should be incorporated as a more general provision in the OMA. In addition, Section 14.5(d) of the OMA should be revised to allow PSEG to terminate the OMA if after 2 consecutive Contract Years PSEG and PREB fail to agree on whether actions taken by PREB satisfy this standard.
11. Change of Control and Acceptable Operator Security: In the November 15 draft of the OMA the term "Acceptable Security" was deleted and the defined term "Guarantee" was inserted in its place. Given the definition of "Guarantee," which is used in the Change of Control definition, this made the Change of Control provision unreasonably restrictive in that the original Guarantor is required to remain the Guarantor through the term of the OMA and there is no provision for a substitute Guarantor. We believe that this was not intended. We would propose that: (i) the term "Guarantee" be revised as follows: "means a guarantee agreement between Guarantor and Owner substantially in the form of Exhibit D (form of Guarantee Agreement), (ii) the term "Guarantor" be defined as follows: ". . . duly organized and validly existing under the laws of [\_\_\_], or a guarantor whose creditworthiness is at least equal to the Guarantor." In Section (D) of the "Change of Control" definition, the language "or any Affiliates of Operator" and Section (E) should be deleted. Also, it may benefit both parties to reinsert the "Acceptable Operator Security" concept so alternative forms of security are not precluded in the future.
12. Delay Liquidated Damages: Consistent with the revision that was made to Shared Services Agreement in Section 4.2, Delay Liquidated Damages should apply only to those conditions that are solely within the control of PSEG, i.e., those conditions that do not require the agreement of the Parties and/or approval by PREB. Accordingly, in addition to moving Sections 4.2(e) (Initial Budgets) and 4.2(f) (Performance Metrics) (see above), please move Section 4.2(i) (Back-End Transition Plan) to either Section 4.1 or 4.5.
13. Use of PSEG Affiliates for O&M Services: In order to fully utilize the capabilities of PSEG and its affiliated companies, affiliate personnel should not be treated as Subcontractors under the OMA. The OMA should explicitly allow for PSEG to use affiliate personnel to provide ServCo related O&M Services (at their hourly fully allocated cost rate without mark-up and that these costs would be a T&D Pass-Through Expenditure). This is the manner in which we intend to provide these services. A simple example is we would have to upgrade the ERP system (and many other IT systems) that PREPA currently uses. We would intend to leverage our IT platform and team in New Jersey to do this work, at cost, which will be much more cost-effective and bring the full suite of tools that we use to manage utilities. Moreover, there should be no restriction on the use of such personnel by the ManagementCo as any of the costs are the responsibility of the ManagementCo.
14. Use of Quick Start Team and Fee at Risk Until Effective Date: In its RFP response, PSEG proposes that the OMA recognize that PSEG will start work immediately upon selection and if the Effective Date occurs that PSEG be compensated for work done prior to the Effective Date as a Front-End Transition Service. If the Effective Date does not occur the PSEG recognizes that it will be at risk for these costs.

15. Minimum Performance Threshold Default: A Minimum Performance Threshold Default under Section 14.1(k) will not be applicable until after the second Contract Year. PSEG requires this because the three (3) Key Performance Metrics will not be set until after 2 Contract Years of operations.
16. Act 120 reference: We understand that the \$0.20/kWh rate in the law has been interpreted by P3 as “aspirational.” This interpretation should be memorialized in the OMA and if the interpretation were to change that would be a “Change in Regulatory Law.” Our concern is that this is an existing law and the enforcement of it would otherwise not be a Change and \$0.20/KWh rate is insufficient to fund the proper operation of the system.
17. Genco: The Shared Services Agreement is between PREPA/P3 and Genco. The costs incurred by ServCo in providing the Shared Services should be included in the Operating Budget and funded by PREPA as a T&D Pass-Through Expenditure. The Service Fee paid by Genco for the Shared Services should be remitted to PREPA.
18. Limitation on use of Insurance Proceeds: Changes made to Section 10.3 in the November 15 OMA draft would appear to require that insurance proceeds be used only for “remediation” of T&D System subject approval of P3. This requirement should apply to insurance proceeds related to Losses to the T&D System but not to Losses associated with the O&M Services. We believe this was unintentional.
19. Credit Downgrade: A new clause was included in Section 7.8 of the OMA that in the event of a PREPA credit downgrade PREPA is required to increase funding of the service accounts but has up to 6 months to restore the accounts to the 4.5 months of anticipated expenses. This is unreasonably long and we would suggest no more than 3 months. Further, if PREPA fails to increase funding in the accounts within the restoration period this should be an event of default under Section 14.3(f)(failure to fund Front-End Transition Account or Services Account) of the OMA. There should be no reference to the securitization entity rating since it is not an indication of PREPA’s creditworthiness.
20. Termination for failure of Conditions to Operations Services: There is new language added to Section 4.8(b)(iii). We are not clear why this change was made and request clarification. PSEG should be able to terminate the OMA nine (9) months after the Target Service Commencement Date regardless of any allegations of fault relating to any outstanding conditions precedent.
21. Failure to Pay Services Fee: The Operator’s obligation to provide or continue to provide Back-End Transition Services is conditioned (in Section 16.2(a)) on PREPA paying the Service Fee.
22. IP Representation/Warranty: Sections 19.1(j) and 19.2(h), representations/warranties regarding IP, now include an absolute representations/warranties that Operator IP and Owner IP do not infringe third party IP, which was not present in the language we proposed or the LIPA Agreement. This representation and warranty must be qualified by knowledge.
23. Review Cycle Time During Front-End Transition: PSEG is proposing the Targeted Service Commencement Date be January 1, 2021. We understand the Government of Puerto Rico’s strong desire for a Commencement Date in 2020 and PSEG will work collaboratively with PREPA and PREB to find opportunities to advance the Service Commencement Date. In order to advance this date, PSEG suggests that the OMA be modified to require that the review/approval period for conducting the Administrator and PREB reviews be done in parallel. This will reduce

cycle time by one month or more for the following items: (i) System Remediation Plan (Section 4.1(d)(iii)), (ii) System Operations Principles (Section 4.1(h)), (iii) Performance Metrics (Section 4.2(f)), (iv) Initial Budget (Section 4.2(e)), (v) Federal Funding Procurement Manual (4.1(e)(ii)) and (vi) Non-Federal Procurement Manual (4.1(f)(ii)). Further, Section 6.1(a)(v)(Rights and Responsibilities of Administrator) should be modified such that during the Front-End Transition, that with regard to the above items, the Administrator should respond to PSEG's data requests within 5 days of such requests.

24. Conforming Changes: The OMA also requires a number of changes to make it executable by the parties; such changes are by way of clarification (including clarification regarding the treatment of certain taxes), conforming and typographical in nature.