VIRGIN ISLANDS
WATER
AND POWER
AUTHORITY

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VIA ELECTRONIC MAIL

Dear Senator Frett-Gregory:

Please see my testimony below for the April 24, 2024 Committee on Budget, Appropriations, and Finance meeting.

Regards,

Andrew L. Smith

Testimony

I am Andrew L. Smith, Chief Executive Officer and Executive Director of the Virgin Islands Water and Power Authority, which I may refer to as WAPA or the Authority. I would like to thank the Honorable Chair, Senator Frett-Gregory, as well as other members of the Senate present for the opportunity to appear before you today to discuss WAPA's current financial crisis and associated recent rotating power outages.

Transparency and Disclosure

Reference was made in yesterday's press conference to information that the Legislature has requested about WAPA and not received. WAPA has not received any requests for information since its last appearance before this body, but we are providing a packet of financial information today. If there is additional information regarding WAPA's financial position desired by the Legislature, please let the Authority know what information is being sought and WAPA stands ready to provide that information.

Where WAPA's Money Is Spent

Before addressing the current financial crisis at WAPA, I want to describe WAPA's typical monthly revenues and expenses. WAPA manages a budget just like any household. An individual earns money for doing a job, and the money earned must cover rent, food, water, medicine, and other necessities of life. Any money leftover can be spent on other things.

In the case of WAPA and its cash flow, WAPA typically collects $21 to $23 million each month in cash from its customers, and the rate WAPA charges its customers is WAPA's only source of cash. WAPA's monthly fuel bill is typically $16 to $18 million, so approximately 80% of WAPA's cash is spent to pay for fuel each month. After paying for fuel, WAPA pays its employees, which costs approximately $2.5 million per month. The combination of fuel and payroll consumes approximately 90% of WAPA's cash each month. The remaining amount of cash, or approximately $2.5 million, must satisfy all WAPA's other financial obligations.

WAPA's other large obligations include payments to Seven Seas Water, who makes drinking water, and charges approximately $1.1 million per month, Aggreko, who leases generation to WAPA on St. Croix, and charges approximately $800,000 per month, and debt service, which is approximately $2.8 million per month. In addition, WAPA must weigh payments to other vendors for various goods and services.

WAPA's Current Financial Crisis

The financial crisis at WAPA has been precipitated by three primary events. One, an increase in the cost of propane supply to the Territory, two, non-payment by WAPA's largest customer, and three, shielding the community from the high cost of electricity.

Cost of Propane Supply

WAPA's largest cost is paying for fuel, which accounts for approximately 70% of total costs. The cost that WAPA pays for propane consists of two components: the cost of the propane itself and the cost to transport propane to the Territory. The cost of propane is based on the market price for propane, which fluctuates. The cost of transportation of propane to the Territory is contractual. That rate was $0.38 per gallon prior to the suspension of propane supply to the Territory in late 2022. When propane supply resumed to the Territory in early 2023, that transportation rate was increased to $0.68 per gallon, an increase of 80%. The cost of transportation of propane to the Territory was increased again in January 2024 to $0.71 per gallon, an increase of 87% versus the $0.38 legacy contractual rate. The cost of propane transportation to the Territory at $0.38 per gallon is approximately $2.6 million per month. The cost of propane transportation to the Territory at $0.71 per gallon is approximately $4.9 million per month. At the increased rate, WAPA is paying approximately $2.3 million more per month for propane transportation than it was under the legacy contract. To put $2.3 million in context, WAPA's total monthly revenues are approximately $21 million, so over 10% of the revenue it collects from customers is consumed by this higher cost.

The increased transportation cost has been borne by WAPA for 16 months and totals approximately $37 million.

Non-Payment by WAPA's Largest Customer

The central government and government component units are collectively WAPA's largest customer and represent approximately 25% of WAPA's revenue. The payment performance of WAPA's largest customer started to deteriorate in June 2023, and the amount of past due payments owed to WAPA for previously provided electric and water services reached $24.2 million at the end of February 2024. The outstanding past due balance has not declined materially since then.

To put the impact of non-payment in context, I noted earlier in my testimony that WAPA's typical monthly revenue is approximately $21 million. The amount owed by WAPA's largest customer exceeds more than one month of the Authority's total revenue.

WAPA converts over 98% of the amounts billed to non-government customers into cash. That is primarily because WAPA disconnects service for non-payment. WAPA has taken similar steps to try and address non-payment by its largest customer. WAPA cannot disconnect customers that provide critical services to the Territory, the hospitals for example. However, WAPA did issue disconnection notices to government agencies that do not directly impact health, safety, and welfare. That has resulted in some additional collections.

Shielding the Territory from the High Cost of Electricity

WAPA's residential rate charged to customers is $0.41 per kilowatt hour (kWh). Its true cost of producing electricity is $0.55 per kWh. As a result, WAPA loses money on every kWh of electricity that it sells. That is partly due to the inefficiency of some of WAPA's generation, which I will describe later in my testimony; however, WAPA's high production cost is also due to the market price of fuel. For example, diesel is 79% more expensive today than it was at the beginning of 2021, and propane is 9% more expensive than it was at the beginning of 2021. Prices for both commodities were already elevated at the beginning of 2021, so the price increases just referenced are versus a starting point that was already relatively high. WAPA has not passed any of these costs through to customers. If WAPA passed its true cost through to its customers, the average customer would pay approximately $750 more per year for electricity.

WAPA held its rates flat when almost every other utility in the Caribbean increased rates. Rate increases across the Caribbean over the past three years have averaged 46%. WAPA's rate is currently about average among its peers.

WAPA shielded its customers from the high cost of fuel in part with support from the Government of the Virgin Islands; however, that fuel support ended in June 2023. WAPA has absorbed its higher cost versus its rates since then.

Public Disclosure of its Financial Stress

It's crucial to convey the gravity of WAPA's financial situation while also emphasizing the proactive steps taken. The Authority has been transparent about the financial challenges for months both in public statements as well as in private meetings. For example, the Authority met with members of the 35th Legislature in December last year to outline the amounts owed to the Authority from the Government. However, the severity of our predicament might not have been fully conveyed despite the Authority's efforts.

The Authority foresaw this difficulty coming as was seeking a collective sense of urgency to avert the current situation, which now threatens the stability and resilience of the electric grid across the Territory. It's important to note that we've been proactive in our conversations with this body, our stakeholders, and our customers. Despite these efforts, the Authority finds itself in a critical position.

Moving forward, we remain committed to addressing these challenges head-on and working collaboratively to navigate through these financial difficulties.

Recent Rotating Power Outages

WAPA cannot spend money that it does not have. Starting in the second half of last year, WAPA had to increasingly defer vendor payments in favor of making payments for basic operating expenses. The strategy to defer vendor payments was in anticipation of two key strategic initiatives being completed by the end of last year. One, the closing of the acquisition of the Propane Supply Infrastructure from Vitol, and two, the new Wartsila generators coming online on St. Thomas. The completion of both initiatives was delayed as I will describe later in my testimony. As WAPA's cash was depleted, two events led to rotational power outages last week.

St. Thomas Diesel Supply

WAPA deferred payment for a supply of diesel for St. Thomas to be able to pay for a shipment of propane when it did not have enough cash to pay for both at the same time. Rotating outages on St. Thomas would not have been necessary just because of the delayed payment for diesel; however, bad weather moved into the Territory leaving the diesel barge unable to leave port from Puerto Rico. Before the weather improved, and the barge was able to sail to St. Thomas, WAPA was forced to enter a rotation outage schedule on St. Thomas that commenced at noon on Friday, April 12 and ended mid-morning on Sunday, April 14. WAPA took these steps proactive to prevent longer, more widespread outages district-wide, while prioritizing electric service for essential community service like the hospitals.

St. Croix Leased Generation

WAPA has four generators on St. Croix, one of which WAPA leases from Aggreko. The Aggreko generators represent about 50% of the generation WAPA uses during most hours of the day when WAPA has two generators online. However, WAPA needs three generators online to meet peak electricity demand during certain hours of the day. One of WAPA's four generators, Unit 19, is temporarily out of service for maintenance, so WAPA currently only has three available generators on St. Croix. The Aggreko lease payment is one of WAPA's larger fixed costs and was a payment that WAPA was deferring in order to pay for fuel, payroll, and debt service. In response to the growing past due balance, Aggreko notified WAPA that it would suspend service for non-payment. WAPA had no ability to pay, and service was suspended at five pm on Monday, April 15. WAPA had to start rotating outages during peak demand hours with only two remaining operating generators available. This schedule of rotating outages was also undertaken to ensure that essential services were not impacted.

Government House contacted Aggreko on Thursday, April 18 and Aggreko returned the generators to service on the morning of Friday, April 19.

A Path to Sustainability – But Repeatedly Delayed

WAPA has a plan to right-size its cost structure so that it can live within its regulated rate. Two key strategic initiatives that have the most significant impact are the closing of the acquisition of the Propane Supply Infrastructure from Vitol and the new Wartsila generation coming online on St. Thomas.

Acquisition of the Propane Supply Infrastructure from Vitol

The application for grant funding for the acquisition of the Propane Supply Infrastructure has been with HUD since June 2023, and WAPA continues to work with the Virgin Islands Housing Finance Authority on completing the process for grant funding; however, grant funding keeps getting delayed despite efforts by the Authority to advance the process.

Placing the Wartsila's in Service on St. Thomas

The new Wartsila project on St. Thomas, funded by a grant from HUD, was close to completion when Wartsila demanded payment of $15 million for change orders. If it was not paid, Wartsila told WAPA it would stop work on the project. WAPA had already agreed to some of the change orders, was requesting documentation on other change orders, and was disputing some change orders. That was part of WAPA's regular due diligence to ensure that the Territory was receiving value for its investment. WAPA's due diligence was also because a portion of the requested change orders, approximately $5 million is eligible for HUD reimbursement, but requires the appropriate documentation.

WAPA has been in negotiations with Wartsila about a return to work, and we hope to conclude negotiations soon; however, these negotiations have substantially delayed the project.

Putting WAPA on a Path to Sustainability and Ultimately Rate Reduction

These two initiatives alone are expected to save the Authority about $5 million per month, or almost 25% of its typical monthly revenue. A monthly savings of $5 million stabilizes WAPA financially and places the Authority in a position to live within its currently approved regulated rate.

This critical foundational cost savings creates a financially sustainable Authority and establishes a platform where additional savings can be captured and can position the Authority to reduce its rates.

Additional cost savings initiatives include:

- Solar and battery storage projects. These are already under construction on St. Croix.
- Wind energy. The lease for site control has been completed and awaits execution.
- Replacement of the rented Aggreko units with owned generation. Generation has been identified, but funding needs to be secured.
- Replacement of inefficient generation on St. Croix with modern, efficient generation. Generation has been identified, but funding needs to be secured.
- Conversion of Unit 27 on St. Thomas to propane. The equipment has been identified and is available. Funding needs to be secured.
- Launch of the AMI replacement RFP. Currently being reviewed by FEMA.

This concludes my testimony. Again, I thank the Senate and the public for the opportunity to discuss WAPA's current financial situation and its path forward. I would also like to thank the hardworking men and women who work around the clock, regardless of weather, daylight, or nighttime in the WAPA family.