national
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guarantee

DEMYSTIFYING THE PREPA TRANSACTION

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Introduction

In February 2016, the Government of Puerto Rico approved legislation to allow the Puerto Rico Electric Power Authority ("PREPA") to restructure its debt. The approval is a critical first step towards the finalization and execution of the Restructuring Support Agreement ("RSA") that was negotiated among PREPA and its creditors.

The proposed transaction has many components to it and includes various parties with different interests, but its overriding goals include helping PREPA achieve a more efficient capital structure and manage its liquidity position while giving the citizens of Puerto Rico the lowest possible cost of energy and minimizing the impact on creditors.

This summary attempts to explain some of the more significant features of the restructuring transaction terms and benefits to each party.

Transaction Overview

- National Public Finance Guarantee ("National") and Assured Guaranty ("Assured"), together, the "Monolines");
- a group of uninsured bondholders representing approximately $3.2 billion, or 39.0% of PREPA's power revenue bonds (the "Ad Hoc Group"); and
- Scotiabank (in its capacity as administrative agent of the Scotiabank Lenders, "Scotiabank"), and Solus (together with Scotiabank, the "Banks").

On December 23, 2015, these parties entered into the RSA with PREPA addressing, among other things, the treatment of approximately 65% of $8.1 billion of outstanding PREPA bonds and approximately $700 million of fuel-line loans.

As detailed below, the restructuring transaction prevents a default by PREPA and provides PREPA with deleveraging, reduced short-term demands on its cash flow and immediate liquidity. For its part, PREPA has agreed to support these transactions and reform its rate-making process. As part of the restructuring, a new special purpose entity ("SPE") with the power to impose and collect a charge from customers connected to the electric system, will exchange its own bonds for existing PREPA bonds on the terms set forth in the RSA and further described below. Customers of PREPA will benefit from a financially stable utility that should have improved access to the capital markets to fund critical investments in infrastructure. The restructuring transaction will provide the Monolines and the Ad Hoc Group with an enhanced security package that will be facilitated by a securitization of the additional revenues created by the "transition charge" on customers' bills. Each Bank has the option of exchanging into the securitization at a discount or keeping its legacy debt at a more financially stable PREPA.

Key Provisions of the Restructuring Agreement

At the heart of the RSA is the SPE that will issue the securitization bonds. The securitization bonds will be secured by a separate, non-bypassable transition charge levied on all PREPA customers. The initial transition charge will be set based on historical usage and in an amount sufficient to cover debt service due on all securitization bonds. A regularly scheduled (likely to be quarterly) "true-up" analysis will determine any adverse impact of delinquencies and usage patterns, and the charge will be adjusted

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Please note that the transaction has not been consummated and final terms may differ from this summary, which is as of March 24, 2016.

to ensure that debt service on the securitization bonds can be adequately covered. A third-party calculation agent will monitor this adjustment process.

In order to achieve an investment grade rating for the securitization financing, a significant debt service reserve fund ("DSRF") of up to 10% of the securitization size is required. The Monolines have agreed to fund a portion of this DSRF with a surety bond, materially reducing the potential cost of the securitization and increasing the likelihood of a successful debt issuance. The Monolines have agreed to provide surety bonds of up to $462 million which will be drawn upon, if necessary, after a $65 million cash-funded DSRF. The Monoline legacy bond exposure at PREPA will benefit from the securitization through the pledge of securitization bonds ("Mirror Bonds") in the same principal amount, interest rate and amortization profile as the currently outstanding and insured legacy bonds. The holders of bonds insured by the Monolines will not be exchanging their bonds, as they will continue to receive regularly scheduled interest and principal payments on the relevant payment dates through payments by PREPA or under the Monoline insurance policies.

The Ad Hoc Group's participation in the RSA provides PREPA with deleveraging, near term cash flow relief, and immediate liquidity. Deleveraging is achieved by the Ad Hoc Group's agreement to exchange their existing bonds at 85% of par for newly-issued securitized bonds, resulting in an immediate reduction of PREPA's debt burden by approximately $600 million. The new securitization bonds will be interest-only for the first five years, providing PREPA with further cash flow relief. Collectively the Ad Hoc Group and Monolines will provide immediate liquidity relief to PREPA via their commitment to purchase $111 million of new PREPA bonds, subject to certain funding conditions precedent. These bonds will earn 10% interest, will mature on 7/1/19 and, in the case of the Monolines, will be economically defeased by the pledge of a like amount of Mirror Bonds when the SPE issues its securitization bonds.

The uninsured bond holders not part of the Ad Hoc Group, representing approximately $2.8 billion (35%) of PREPA's $8.1 billion of outstanding bonds may voluntarily exchange into the securitization on the same terms as the Ad Hoc Group and receive the additional protection and ratings increase offered by the securitization structure. As a condition to PREPA closing the transaction, bondholders in this group representing at least $2.1 billion of the remaining $2.8 billion outstanding must opt into the securitization. Non-exchanging uninsured bondholders will remain as legacy debt of PREPA.

The Banks have almost $700 million of loans that are currently due and payable by PREPA. The Banks have the option either to: (1) amortize their debt over six years and reduce the default rate of interest by 150 basis points; or (2) convert their current claims into securitization bonds on the same terms as the Ad Hoc Group exchange. Either election by the Banks will provide cash flow relief to PREPA.

What Comes Next?

While the restructuring transaction passed its first significant hurdle when it was approved by Puerto Rico's House of Representatives and Senate and signed into law by the Governor, as with any transaction of this complexity there are numerous conditions that must be satisfied before the transaction can be completed. Critically, the Puerto Rico Energy Commission must review the method for setting the transition charge that will facilitate the entire transaction and the securitization bonds must achieve an investment grade rating.

Party to Transaction	Gains	Provides
PREPA	- Liquidity - Principal forgiveness/debt relief/deleveraging - Lower interest rates	- Adjustments to electricity rate - Agreement to restructure debt through a securitization
Customers	- Financially stable electricity provider that can obtain funds for critical infrastructure investments	- Adjustment to electricity rate and payment of transition charge
Ad Hoc Group	- Investment grade rating on investment position - Enhanced security structure	- Principal reduction - Liquidity to PREPA through bond purchase agreement, principal reduction and 5-year interest-only period
Monolines	- Enhanced security structure	- Increased exposure through surety policy that enables the securitization - Liquidity to PREPA through bond purchase agreement