Financial Oversight & Management Board for Puerto Rico

Statement regarding memorandum from former Governor George Pataki

(San Juan, Puerto Rico, July 28, 2017)—On June 20, 2017, former Governor George Pataki, senior advisor to the Ad Hoc Group of Puerto Rico General Obligation Bondholders, sent a memorandum to The Financial Oversight and Management Board for Puerto Rico, created by Congress under the bipartisan Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"), and to Governor Ricardo Rosselló, which contains serious allegations regarding the Board's and the Administration's characterization of Puerto Rico's fiscal situation. The Board believes his claims are erroneous. Specifically, the Board wishes to be clear that the Government's liquidity and solvency problems are very serious and represent a situation that requires actions on all fronts to ensure there are sufficient resources to fund essential services to the public and put the budget on a path to structural balance, both specific requirements under PROMESA.

Since their appointments in August of 2016, all seven members of the Board have been working diligently to fulfill their duty and charge under PROMESA for the benefit of the people of Puerto Rico. The certified Government of Puerto Rico Fiscal Plan, approved by the Board on March 13, 2017, in addition to structural reforms aimed at fostering economic growth, contains substantial expenditure cuts and revenue increases in an effort to structurally balance the budget and foster sustainable debt service. However, given the expiration of the stay against litigation provided under PROMESA on May 1, 2017, Title III became necessary to protect the people of Puerto Rico and avoid further negative impact on the economy from a flurry of litigation and continued uncertainty.

Under PROMESA, the Government of Puerto Rico, with the Oversight Board's support, has pursued voluntary negotiations and mediation in an effort to arrive at consensual agreements with its creditors. In fact, the Oversight Board continues to believe that consensual negotiations are preferable to the extent possible and will pursue them with all creditor groups willing to do so. Title III filings do not bring an end to those discussions.

The chart below contains the Board's clarification of specific erroneous claims made in Governor Pataki's memorandum.

Claim contained in Pataki Memo	**Fact**
"The Oversight Board and the Commonwealth approved a plan that openly violates PROMESA by elevating all government expenses above all debt service, regardless of lawful priority."	On March 13, 2017, the Board considered the Governor's proposed fiscal plan, following substantial deliberations and discussions with experts, consultants, and attorneys. After substantial deliberations, the Board certified an amended fiscal plan, compliant with PROMESA. Further, the fiscal plan first reduces spending and increases revenue to the maximum extent possible without compromising growth prospects with the intent of putting Puerto Rico back on the path of fiscal sustainability. The remaining surplus could then be allocated to other priorities, including, among other things, debt service. The Board's economists have advised that further spending cuts or revenue increases beyond those in the plan would undermine Puerto Rico's long-term economic growth potential and ability to achieve sustainable fiscal balance. The purpose of increasing revenues and cutting expenses is to restore fiscal balance so that Puerto Rico can fund essential services, pensions, capital expenditures to support economic growth, while respecting relative priorities, and to pay for sustainable debt, consistent with PROMESA.
"The Oversight Board has made clear that it is unwilling to consider input from creditors about inaccuracies contained in the fiscal plan…by its refusal to engage with creditors in any meaningful way, the Oversight Board forced the Commonwealth into a completely preventable bankruptcy."	The Oversight Board and government held more than 30 meetings with creditor representatives from December 2016 through March 2017. Its advisors considered observations made by creditor groups at these meetings in formulating its economic model. On March 13, 2017, the Board certified an amended version of the governor's plan,

	which included for the first time a debt sustainability analysis, necessary to determine how much debt service the government could afford to pay.
“the Board and Commonwealth refuse to provide a satisfactory answer to Members of Congress that have expressed concerns over the Fiscal Plan’s unlawful treatment of priorities…”	The Oversight Board has addressed and replied to each and every communication submitted by Members of Congress to date (correspondence is available for review at the Board’s website www.oversightboard.pr.gov) and Board members have made themselves available to testify before Congress on matters pertaining to the Fiscal Plan. The Board continues to be available to engage with Members of Congress and their staff interested in discussing its progress.
“The Rosselló Administration is refusing to respect payment priorities as required by PROMESA.” “The budget includes year over year public expenditure increases of $575 million…” “In total, the FY 2018 budget represents a year over year increase of 6.4% in total non-debt-related expenditures.”	The final FY18 budget was approved by the Board on June 30, 2017 and is both compliant with PROMESA and generally consistent with the fiscal plan. In fact, spending in the FY 18 general fund budget is actually 9% lower than the FY 17 budget once additional pension funding is excluded. This new funding is required because the retirement system are out of liquid assets and must convert to pay-as-you-go.
“States pay their debts. Governor Rosselló is asking Congress to grant statehood to Puerto Rico despite his refusal to honor Puerto Rico’s own constitution or lawful commitments to millions of American citizens in Puerto Rico and the mainland who own constitutionally-protected bonds as part of a retirement fund.”	No state has ever had a debt burden that is even close to that of Puerto Rico, by any measure. Puerto Rico has approximately $74 billion of debt and another $48 billion of unfunded pension liabilities. Puerto Rico’s net tax supported debt as a percentage of 2017 GDP is 55.1% compared to 9.2% for Connecticut, which has the highest percentage among states. Furthermore, states have significantly more access to federal funds compared to amounts available to Puerto Rico and other territories.
“The Board insists on projecting a decrease in the Commonwealth’s revenues and a contraction in the island’s	Puerto Rico’s economy is in a structural decline with real

GNP, in spite of contradictory information. Puerto Rico's revenues are up, powered by robust consumer consumption. Both tax collections and nominal GNP are at all-time highs."	GNP declining every year but one for the past decade. The last official actual data on real GNP growth is for 2016 and shows a decline of -1.1% and the negative trend is expected to continue. There is also additional austerity on the horizon further pressuring growth prospects. Revenues are up, but this is because tax and fee increases which are placing an additional burden on the people. For example the sales and use tax was recently increased to 11.5%, the highest among all the states. Even more worrisome is that expenses are forecast to increase significantly faster than revenues as Puerto Rico hits several fiscal cliffs. Despite negative real GNP, the Commonwealth does forecast moderate revenue growth in its projections based on the proposed policy actions in the fiscal plan including improved tax administration and excise tax adjustments.
"The Oversight Board uses these misleading projections to argue the island has the capacity for only $400 million in debt service in the coming year. In fact, before pension payments, the Commonwealth is running a primary surplus of $3 billion for FY18. It also has $1 billion less in accounts payable – spread over multiple years – than had previously been forecast by the Fiscal Plan."	This assertion flagrantly disregards Puerto Rico's fiscal reality. Achieving the primary surplus balance described depends on erroneous, fallacious, false assumptions. One would have to stop paying all retirees their pensions, halt supplier payments, and delay the provision of other essential services to achieve the primary balance described. Protecting the social safety net and critical operations is paramount as the economy would otherwise never recover.
"As of June 30, the Commonwealth is expected to have a cash position of $1.15 billion, compared to $291 million forecast in the Fiscal Plan…"	The cash balance in the government's bank account at a particular moment in time does not accurately reflect Puerto Rico's overall liquidity situation, but instead reflects the seasonality of revenues and expenditures as well as the delayed payment of many liabilities and one-time cash

	flows. The Commonwealth faces $2.3 billion of fiscal cliffs in FY18 and expenses outpace revenue in the first half of FY18.