

**FINANCIAL OVERSIGHT AND MANAGEMENT BOARD  
FOR PUERTO RICO**



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**SENT VIA ELECTRONIC MAIL**

March 8, 2017

Honorable Ricardo A. Rosselló Nevares  
Governor of Puerto Rico  
La Fortaleza  
PO Box 9020082  
San Juan, PR 00902-0082

Dear Governor Rosselló Nevares:

Thank you for submitting the Government of Puerto Rico's proposed Fiscal Plan on February 28<sup>th</sup>. We commend your efforts in such a compressed timeframe to analyze and address the fiscal situation of Puerto Rico and to develop your approach to tackle this challenge. Even as we continue to analyze the Fiscal Plan we want to bring to the forefront our concern regarding the current liquidity situation. We believe that without major emergency actions the Commonwealth soon will be unable to pay essential services, including pensions, education, healthcare and public safety, in a matter of months. This requires our collective and immediate attention.

The Board commissioned a report from Ernst & Young on the Government's bridge between the 2014 audited financial statements and the 2017 fiscal plan baseline numbers. This report was completed and presented today, and a copy of it is attached. The report's conclusion is that the Government's fiscal year 2017 expenditures could be understated by an amount ranging from \$360 to \$810 million based on historical expenditure trends.

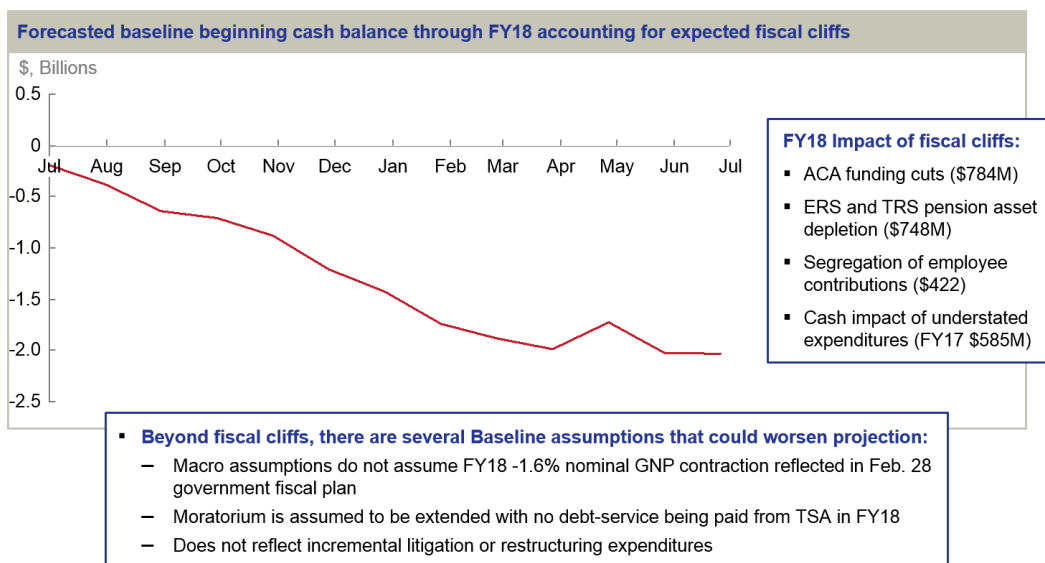
The Commonwealth's liquidity projections do not reflect these historical trends. Based on the midpoint of the range of potential understatement of expenditures, the Board estimates that the Commonwealth could face a cash deficit of approximately \$190 million by the beginning of July 2017. The Commonwealth will face this reality, having already defaulted on its debts, having no access to the capital markets on normalized terms and having exhausted many extraordinary cash management measures. In addition, before the end of calendar year 2017 the Employee Retirement System ("ERS") pension fund will be depleted, the Teachers Retirement System ("TRS") fund will be depleted, and the government will begin the overdue segregation of

employee contributions, requiring the Commonwealth to make approximately \$1.2 billion in pension payments out of its operating budget.

The Commonwealth will also lose approximately \$800 million of Affordable Care Act funding for its healthcare system during the fiscal year 2018, beginning in the end of calendar year 2017.

## EXHIBIT 1

### Baseline FY18 liquidity projection forecasts ~(\$2B) ending cash balance



While we appreciate your focus on addressing Puerto Rico's long-term fiscal and economic challenges, we think far more needs to be done immediately to reduce spending and avoid this critical cash shortfall. Given Puerto Rico's lack of normal capital market access and our need to focus on a sustainable restructuring of debt it is neither practical nor prudent to address this cash shortfall with new short-term borrowing.

Even assuming nonpayment of debt, and expeditious implementation of cash and budgetary measures included in your Fiscal Plan, we believe the following is required:

- Immediate implementation of a furlough program to achieve \$35-40 million in monthly savings, through the equivalent to 4 days per month for most Executive branch government personnel and 2 days per month for teachers and frontline personnel at 24-hour institutions. Frontline law enforcement personnel should be exempted from the furlough program.

- Reductions comparable to the Executive branch furlough savings described above for other entities across the government, including public corporations and instrumentalities and the Legislative and Judicial branches.
- Reductions in professional service contract expenditures of up to 50 percent and significant reductions in all Government contract expenditures.
- Reductions in healthcare costs, by negotiating drug pricing and reductions of rates to health plans and providers.

To address the cash crisis, we believe that you should immediately direct AAFAF, in accordance with the authority granted to you under Act 5-2017 and other relevant legislation, to exercise control of all accounts, revenues and expenditures of the Government of Puerto Rico and its instrumentalities in order to implement a new liquidity plan consistent with the guidance in this letter. As you know, AAFAF was created in 2016 as a public corporation and governmental instrumentality independent of the Commonwealth, with fiscal and administrative autonomy. AAFAF was designed to act as fiscal agent, financial advisor, and reporting agent for the Government of Puerto Rico and other public entities and municipalities to assist them in confronting the fiscal and economic emergencies that Puerto Rico now faces. In January 2017, your Administration signed a law expanding AAFAF's powers to include sole responsibility for renegotiating and restructuring public debt.

We also await the additional detailed information requested on the Fiscal Plan and liquidity plan measures.

We remain committed to working with you to address these challenges expeditiously and comprehensively for the benefit of the people of Puerto Rico.

Sincerely,



José B. Carrión  
Chair

Andrew G. Biggs  
Carlos M. García  
Arthur J. González  
José R. González  
Ana J. Matosantos  
David A. Skeel, Jr.

CC: Elías F. Sánchez-Sifontes