WRITTEN TESTIMONY OF

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before the

House Committee on Natural Resources

Oversight Hearing on PROMESA: Discussion Draft

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Chairman Grijalva, Ranking Member Bishop, and Members of the Committee, I am Natalie Jaresko, Executive Director of the Financial Oversight and Management Board for Puerto Rico (the "Board" or "Oversight Board"). Thank you for this opportunity to update the Committee in this hearing on the work the Board is doing for the benefit of the people of Puerto Rico. Since I testified before this Committee on May 2, 2019, the Board has made substantial progress towards achieving its mandate under PROMESA. I also appreciate the chance to comment on the PROMESA discussion draft and the impact of its proposed changes on the Board's work.

I. Introduction

Before PROMESA was adopted, Puerto Rico faced an unsustainable burden of more than $70 billion in debt and more than $50 billion in unfunded pension liabilities, exacerbated by a decade of economic decline and significant outmigration. The sitting Governor had declared the debt was unsustainable and could not be paid, and more than 300,000 people – 10 percent of the population – had already left the Island in search of greater economic opportunity. Nonetheless, government spending remained bloated, government services were inefficient, liquidity shortfalls impaired strategic decision making, and no multi-year, coordinated strategy existed to restore growth and opportunity to the people of Puerto Rico. In 2016, Congress through PROMESA provided a way forward for Puerto Rico.

As the Board got underway with its work, Hurricanes Irma and María inflicted the most horrific natural disaster devastation to strike the U.S. in 100 years, compounding the financial and humanitarian distress to the Island and its people. The Board worked extensively with the Government in joint post-hurricane efforts, including the critical importance of transforming the power sector to be more reliable, resilient, and cost-effective. The Board continues to support the efforts of the Puerto Rico Government and the U.S. Government to provide the critical disaster relief funding to the Island and its residents.

This summer the people of Puerto Rico spoke clearly about their demands for better governance and more responsive government services. The resignation of Governor Rosselló was complex and disruptive to the ongoing work of the Puerto Rico Government for the Island and the people of Puerto Rico. However, it did not deter the Board in carrying out its obligations under PROMESA and persisting in its work to assure the efficient and effective delivery of those important government services. The Board has continued to work with the elected leaders of Puerto Rico to provide its people with the stability needed by all stakeholders. Since Governor Wanda

Vázquez took office on August 7, the Board has engaged in a collaborative, working relationship with the Governor and her team. In addition to three working meetings of the Governor and the Board, the Board has held dozens of meetings with the Governor's team on fiscal plan and budget implementation. We have made great progress working together, despite ongoing differences which remain.

As you know, a significant aspect of the Board's responsibility for administering the largest public entity restructuring in U.S. history includes defending against nearly one hundred lawsuits filed in opposition to the Board's certified fiscal plans and budgets formulated to carry out PROMESA. Predictably, those creditors dissatisfied with the proposed Plan of Adjustment the Board recently filed are also gearing up to launch challenges to the Board's plan proposal. The Board continues to try to resolve these disputes as fairly and expeditiously as possible consistent with the mandates of PROMESA. The Board also continues to monitor more than 120 reform implementation plans the Board inserted into its certified fiscal plans, necessitating hundreds of working meetings with the Government and Legislature, and numerous hearings, as well as town hall meetings across the Island with members of the public.

The month of September was of particular significance for the Board's work. Last month we filed our proposed Plan of Adjustment for the Commonwealth and a proposed disclosure statement explaining it. This filing is a major milestone for the Board, as it addresses over $35 billion of debt and other claims against the Commonwealth of Puerto Rico, the Public Buildings Authority (PBA), and the Employee Retirement System (ERS), and more than $50 billion of pension liabilities, and represents the beginning of the end of the bankruptcy-like state that Puerto Rico has been in since 2017. I will discuss the proposed Plan of Adjustment in detail further in my testimony.

I will now cover the Board's main accomplishments since my previous testimony in the areas of debt restructuring and fiscal plan implementation and responsibility.

II. Debt Restructuring and the Plan of Adjustment

On September 27, after years of extensive negotiations, the Board filed its proposed Plan of Adjustment (the "Plan") to restructure $35 billion of debt and other claims against the Commonwealth of Puerto Rico, PBA, and ERS, and more than $50 billion of pension liabilities.

The Plan has five main elements of debt restructuring: the debt of the central government, the debt of PBA, the debt of ERS, claims against the Commonwealth alleging wrongful clawback, as well as general unsecured claims against the Commonwealth, PBA, and ERS. Combined, those elements comprise about $35 billion in debt and claims, which the Plan seeks to haircut by more than 60%.

The Plan would significantly reduce debt service from $82 billion over 30 years to $44 billion. Together with the debt of COFINA, which the Board restructured earlier this year through the Title III process, the amount the Government would have to spend on servicing its debt would fall from a maximum of $4.2 billion a year to $1.5 billion a year – a substantial reduction that leaves Puerto Rico with an amount it can sustainably afford over the next 30 years.

The proposed Plan has 10 key points:

1. Reduces $35 billion in Commonwealth liabilities to $12 billion.
2. Ensures sustainable and affordable annual debt service of less than 9% of government own-source revenue (from 28% prior to PROMESA).
3. Ensures that 74% of current and future pensions are not cut.
4. Establishes a trust supporting pensions for 30 years.
5. Provides predictability to public employees via collective bargaining agreements.
6. Restores $1.3 billion of withheld employee contributions to Sistema 2000, which was until recently a virtually defunct employee-funded retirement benefit fund.
7. Creates a mechanism to settle claims against challenged bonds.
8. Creates a mechanism to eliminate pension cuts to the extent that in any fiscal year the surplus is greater than projected.
9. Allows retail bondholders to elect bonds with monthly interest payments.
10. Establishes a debt management policy to ensure Puerto Rico never again finds itself in this situation.

In sum, this Plan represents a series of compromises on the part of various stakeholders who all recognize the need to move Puerto Rico out of Title III and toward a future of prosperity. All supporters of this Plan have compromised for the good of Puerto Rico.

A. PROMESA Requirements for Confirmation of the Plan:

It is important to remember that PROMESA requires that the Title III Court confirm the Plan before it can become effective. For example, the Court must conclude that the Plan is feasible and in the best interests of creditors collectively. The Board believes this Plan is feasible and in the best interests of all creditors because it restructures Puerto Rico's debt and pension liabilities in a way that provides reasonable compensation to creditors without endangering Puerto Rico's fiscal future, while ensuring pensions and enabling Puerto Rico's renewed growth and investments needed to prosper. Without satisfying these legal requirements, Puerto Rico cannot exit Title III. That is why consensual support from retirees, public employees and bondholders is helpful to lifting the cloud of bankruptcy that endangers Puerto Rico's future well-being. With the support of these groups, the Board demonstrates that it has struck a fair balance in the best interest of all parties for a realistic restructuring Puerto Rico can afford.

B. Stakeholder Support of the Plan:

The Board has, after months of rigorous negotiations, secured the support of three significant stakeholder groups for the Plan:

- the Official Committee of Retirees (COR), which represents retired government employees;

- a group of current government employees represented by the Public Service Union, the Puerto Rico chapter of AFSCME; and

- the Lawful Constitutional Debt Coalition (LCDC), a group of investors and funds who hold Puerto Rico's general obligation bonds and PBA bonds.

C. Public Employee Retirees:

Consistent with the consensual plan support agreement reached with the Official Committee of Retirees, the Plan restructures pension liabilities for the long-term, protects more than 74% of current and future retirees from any reduction, and ensures a reasonable reduction in pensions overall. Pensioners are considered unsecured creditors under the Title III restructuring process, whose treatment under the Plan will have to be approved by the Court. That makes the Board's consensual agreement with COR an important element of the Plan. The Board agreed with COR to a flat 8.5% pension cut provided that no one will have their total monthly retirement benefits reduced below $1,200. The Board also agreed the Commonwealth would establish a pension reserve fund for the PayGo pension system to support payment of pensions over the next 30 years. Moreover, if in any given year the surplus is larger than projected, 10% of the incremental surplus will be reserved to restore the pension cuts of that year.

D. Public Employees:

As to public employees, the Plan covers over 11,000 active public employees and union members in eight agencies of the Government. The Board and the Public Servants United of Puerto Rico/AFSCME Council 95 ("SPU") reached an agreement that secures collective bargaining agreements, protects workers from further compensation cuts, provides workers with bonuses, and ensures savings projected in the Fiscal Plan. The proposed Plan includes the following benefits for public employees:

1. Collective bargaining agreements will remain in effect for five years, reflecting labor terms in the Fiscal Plan.
2. Guarantees stability in the working conditions of employees and prevents further cuts to workers' benefits.
3. Any bonus or economic benefits to public employees lawfully granted by the Government will also apply to SPU members. This agreement, thus, represents the baseline of treatment of public employees.
4. At least $1.3 billion of employees' contributions to Sistema 2000 will be restored.
5. Signing bonus of $1,000 to all SPU members that ratify the agreement.
6. Employer contribution to medical plan set at $170 per month, rather than the $125 previously proposed.
7. Establishes a $5 million trust for healthcare to support transition of employees for whom $170 per month is below their current benefit.
8. Affiliates may keep the right to negotiate the Single Medical Plan, and they will not have to be changed to the Government's health plan.
9. If Government outperforms the Fiscal Plan, 25% of the excess will be allocated to public employees in that year, incentivizing employees to help the Government work more efficiently.

The Board is seeking to broaden active public employee support for the Plan. As you may know, the Board negotiated a preliminary agreement with the "Asociación de Maestros" (AMPR), represented nationally by the American Federation of Teachers. Unfortunately, AMPR was not able to secure a majority vote in support of the agreement with the Board. The Board is hopeful that the filing of the proposed Plan will encourage AMPR to reconsider engaging with the Board.

For the prosperity of all government employees, it is important to move on, to leave this state of financial distress behind, to build a secure future for Puerto Rico. This secure future can only be built working hand in hand with the public sector employees who are critical to the success of Puerto Rico. For too long, so much was taken away from them. We look forward to continuing our discussions with other unions and groups so that they can also be consensual parts of this process.

E. Bondholder support:

As to the LCDC bondholders, their agreement with the Board includes meaningful reductions of the par value of Puerto Rico outstanding bonds and sustainable, affordable debt service payments over the next 30 years. The Board remains committed to negotiations with additional bondholders who have yet to support Puerto Rico in this effort to secure an affordable level of debt and to rebuild a path to renewed prosperity.

F. Debt Investigation and Challenges:

Under PROMESA, the Board undertook a careful review of any potential legal infirmities of the debt that was issued by Puerto Rico and its various agencies and instrumentalities. A Special Investigation Committee of the Board hired Kobre & Kim to conduct a comprehensive study of Puerto Rico's debt and its relationship to the financial crisis. In light of the Kobre & Kim findings, the Board immediately created a Special Claims Committee to determine whether any of Puerto Rico's debt should be challenged and to bring any other litigation involving the debt. As a result of this review, in January, 2019, the Board, along with the Official Committee of Unsecured Creditors (UCC) objected to the validity of over $6 billion of general obligation (GO) bonds as exceeding the debt limit in Article VI, section 2, of Puerto Rico's Constitution (the "Challenged Bonds"). This includes all GO bonds—bonds backed by the full faith and credit of Puerto Rico—issued by Puerto Rico in 2012 and 2014.

This challenge was followed by other legal challenges, filed by other parties, to additional bond issuances:

- the UCC challenged the validity of approximately $2.1 billion of GO and PBA bonds issued in and after March 2011 as exceeding the constitutional debt Limit;

- the UCC and the Official Retiree Committee challenged the validity of over $3 billion of bonds issued by ERS asserting that ERS lacked the authority to issue the bonds; and

- an ad hoc group of bondholders argued that if the arguments in the Board's objection are sustained, then certain GO and PBA bonds issued from and after 2009 may also be invalid.

These objections are forward-looking, meaning they are to determine whether Puerto Rico must repay obligations on these bonds in the future. To the extent, however, that any debt is determined to be invalid, the Commonwealth may be able to collect back prior payments of principal and interest on invalid debt. Thus, to preserve Puerto Rico's rights, other "backward" looking litigation was initiated by the Board:

- The Board and the UCC filed the "Underwriter Complaint" against over 20 banks, law firms and other parties to recover fees they earned when they helped Puerto Rico and certain of its instrumentalities issue nearly $9 billion of bonds. The Underwriter Complaint alleges that these parties aided and abetted the Government Development Bank's breach of its fiduciary duty to the people of Puerto Rico and, as a result, were unjustly enriched by receiving hundreds of millions of dollars in fees.

- The Board and the UCC filed several hundred complaints against entities to recover payments they received on account of the Challenged Bonds in the Title III cases. The Board also initiated litigation against large bondholders who own at least $2.5 million worth of the Challenged Bonds. If the objections to the validity of the Challenged Bonds are successful, then payments of purported principal and interest may constitute fraudulent transfers that can be recovered by Puerto Rico.

When determining whether to object to the validity of the GO bonds and commence the related litigation, the Board considered its fiduciary responsibility to challenge debt that violates Puerto Rico law. The laws of Puerto Rico limit government borrowing authority for a reason: to prevent the Government and its financiers from obligating Puerto Rico and its instrumentalities, as well as taxpayers and legitimate creditors, to a level of debt that cannot be repaid without sacrificing services necessary to maintain the health, safety, and welfare of Puerto Rico and its people.

G. Final Confirmation of the Plan of Adjustment:

The Board continues to negotiate with other groups to build an even stronger coalition of those willing to step forward and close this chapter of financial distress consensually. There may be amendments to the Plan of Adjustment as the Board brings additional stakeholders to support the Plan. The Board hopes the Title III court will be in a position to confirm the Plan in 2020.

III. <u>Fiscal Plan Implementation and Fiscal Responsibility</u>

The Board's duties and empowerment under Title II of PROMESA, as you will recall, center around the development and certification of multi-year fiscal plans which must balance competing priorities enumerated in the law and review or formulation, and certification of governmental budgets consistent with those fiscal plans.

A. Prioritizing critical spending:

In June 2019, the Board certified fiscal year 2020 budgets for the Commonwealth of Puerto Rico, the Puerto Rico Electric Power Authority, the Puerto Rico Aqueduct and Sewer Authority, the Highways and Transportation Authority, the University of Puerto Rico, and COFINA. All these budgets are in full force and effect.

The total amount of government spending (including General Fund, Special Revenue Funds and Federal Funds) for fiscal year 2020 is $20.2 billion, which is broken down to the following priorities: 21% for health, 17% for education, 13% for pensions paid via PayGo, 12% for families and children, and 5% for public safety.[1] For example, the budget provides for increased salaries (a 30% increase over two years) and benefits for police officers and more funding to purchase bullet proof vests, radios, and vehicles. Moreover, police officers will receive Social Security for the first time in this year's budget to provide them a more secure future retirement.

In addition, the budget raises teachers' and school principals' salaries for the second consecutive year and the salaries of firefighters. Notwithstanding these and other spending increases in priority areas, right-sizing the Government to create more efficient government services continues: professional fees declined by 30% year over year, and redundancy in administration within agencies is being reduced via consolidation of the more than 120 government agencies and public corporations.

As in prior budgets under the Board's oversight, the fiscal year 2020 budget intentionally does not provide for the Government spending all the revenues it collects in the current fiscal year. For example, much of the projected surplus of $2.6 billion is being reserved to protect future pension payments and manage other legacy obligations such as the debt. Given the limited structural reforms agreed upon with the Government and outlined in the Fiscal Plan generate insufficient growth to maintain long term balanced budgets, some of the currently projected surpluses are dedicated to fund PayGo payments for retirees in those years when the Government projects a deficit. This is to ensure that retirees never again have to worry about future governments lacking the resources to fully pay their pension. The only solution to the unfortunate forecast return to deficits is increased commitment to new and additional structural reforms to make the economy of Puerto Rico more competitive and economic development more certain.

Recently, the Board has been working closely with AAFAF and OMB to better understand the Department of Education and Correctional Department needs. Both the Department of Education and the Department of Corrections concluded fiscal year 2019 underspending their budgets, in personnel as well as and capital expenditures in some cases. Thus, more detailed analysis of the actual needs is necessary and underway to determine how funds can be best allocated to priority areas, while ensuring their efficient utilization.

B. Improved Financial Transparency in Government:

The fiscal year 2020 budget includes four sets of major improvements in budgeting practices. First, the Board worked with the Government to provide a deeper level of detail in the budget, detail that had not previously been available to the Legislature or public, enabling a better understanding of how funds are being spent. Second, the consolidated budget is more comprehensive and captures items not budgeted previously, including all cash subsidies, which amount to approximately $428 million in fiscal year 2020. Moreover, the Fiscal Plan calls for the Government to consider limiting tax credits issued each year by capping the notional amount authorized, and including sunset provisions that eliminate the ability to claim unused credits previously issued. The Government also now has the capacity to make decisions around limiting and more selectively targeting tax expenditures based on the recent publication of the first-ever tax expenditures report. Third, the

[1] See the Board's fiscal year 2020 budget presentation at: https://drive.google.com/file/d/1woI5fhb02lfnW4GbF-B4xkgauDarWBSQ/view

published budget resolution includes more detailed specific concepts of spending within the personnel and non-personnel categories for each agency to provide a more detailed look at how the Government uses its funds. Finally, a series of budget controls are established within the budget to improve fiscal responsibility and discipline.

The Government has much more work to do to improve its budgeting practices. The Government still operates with six different accounting systems that need to be consolidated to provide better accountability over spending and visibility in budgeted to actual spend reporting. The Government also needs to finally complete the delayed financial audits for fiscal years 2017 and 2018. Completion of the overdue audits and implementing a process that will ensure best practices in issuance of the audited financial statements going forward (completed within 180 days of the end of the fiscal year) is a critical element of fiscal responsibility.

C. Importance of Disaster Aid

The Fiscal Plan assumes the government of Puerto Rico receives $75 billion in Federal disaster aid funding over more than a decade. This funding is critical to restoring resiliency to the power grid, to rebuilding schools, roads, and other critical infrastructure, and to generating positive economic growth on the Island.

Unfortunately, this federal aid, particularly public assistance funding from FEMA and CDBG-DR funding from HUD, has been slow to obligate and disburse. More than two years after the tragedies of Hurricanes Irma and Maria, very few permanent work projects have begun. This is highly unusual and does not remotely match the timeline from other disasters such as Hurricane Katrina and Hurricane Harvey. Additionally, of the $19.9 billion in CDBR-DR funds allocated to Puerto Rico, only $1.5 billion has been made available and only a fraction of that amount drawn down. Moreover, another $8.2 billion still requires HUD's authorization to release and $10.2 billion requires HUD's publication of notice in the Federal Register.

The rapid and efficient deployment of this funding is critical to meeting fiscal plan targets and long-term recovery prospects.

D. Ensuring Fiscal Responsibility in Municipal Government:

The Board announced its decision in May to require a fiscal plan from Puerto Rico's property tax collection agency, CRIM. Since then, the Board has been working with CRIM to outline a series of measures to improve collections without increased tax rates. The primary goals for the CRIM fiscal plan include strategies to update the property registry, revise the classification and valuation of registered properties, review administrative guidance regarding exemptions and exonerations, and improve enforcement and collection efforts. Notwithstanding ongoing litigation between the Board and the Commonwealth surrounding Act 29-2019, which burdens the Central Government with the municipalities' pension and healthcare costs, the Board seeks to continue working with CRIM to review and certify its fiscal plan in the upcoming weeks.

The Board also designated all 78 municipalities as covered instrumentalities under PROMESA, though it has required a fiscal plan from only ten municipalities at this time. The Board selected these municipalities after considering a combination of factors including fiscal challenges, impact of the reduction of transfers from the Central Government, and their experience implementing innovative and creative initiatives and collaborating with other municipalities. This was a proactive step toward helping the municipalities avoid insolvency, finding a path towards financial stability and economic development, and enabling municipalities to do what they do best: serve the needs of their residents. Following the certification of the CRIM fiscal plan, the Board will proceed with the review and certification of the municipality fiscal plans, including spending efficiency measures, such as intermunicipal shared services arrangements, programs to improve and optimize local revenue collection, economic development guidelines, and decentralization proposals. Throughout this fiscal plan development process, the Board has been visiting the municipalities and working with the Mayors to better understand their realities. Just two weeks ago, for instance, Chairman Carrión and I visited the municipalities of Aibonito and Barranquitas to hear about the successful collaboration between their municipalities and Comerío in the provision of permits and other shared services. I want to personally thank all the Mayors for their commitment to this process.

E. Transformation of the Island's Power Sector:

The Board continues to work with Government on the transformation of PREPA to ensure reliable energy for the residents, more effective and efficient management, as well as lower fuel costs. The Board and the Government are in full agreement that private management of the transmission and distribution system, as well as generation, are key to these improvements. The Board is working collaboratively with the Government on the pending Request for Proposal process for selection of a private operator for the grid and strongly supports the Government's efforts to secure FEMA funding to help with the cost of restoration and reconstruction of an affordable, resilient, and reliable power system that is environmentally compliant and that serves as a driver of economic growth. Selection of this operator and securing this federal funding in the next few months are critical next steps in the modernization of PREPA which is essential to increased economic development on the Island. In order to ensure that PREPA adheres to its Fiscal Plan and the rate-reduction initiatives required, the Board is holding regular meetings with the PREPA Governing Board to ensure the PREPA Governing Board and PREPA management are all aligned.

F. Title V:

On August 12, the Board designated the $5.3 million expansion of the Fajardo Municipal Landfill as a critical project under Title V of PROMESA. The Fajardo Municipal Landfill serves as the primary municipal and commercial disposal site for the north-eastern region of Puerto Rico, serving nine municipalities. Engineering estimates state that the current disposal space would be available for only three additional years, and the expansion represents approximately 20 additional years of operating capacity for this critical infrastructure. The project complies with the fundamental criteria to be considered a critical project and addresses two of the Island's most pressing issues: the need to diversify energy generation and to tackle the solid waste management crisis. During a recent visit, I was impressed with the facility and management's plans for the future. The landfill has a four-megawatt gas-to-energy operation and the expansion will allow the site to reach full capacity.

G. The Board's Operations:

The Board remains a small organization, with a flat hierarchy. One of its organizational goals during fiscal year 2019 was to take advantage of Puerto Rico's incredible talent to build organizational strength through local recruiting, thereby reducing costs and the use of third-party mainland consultants. The overwhelming majority of the new hires are Puerto Ricans, several of whom have returned from the U.S. mainland to help the Island recover. The expenses incurred by the Board in carrying out its mission are substantial and necessary. Nevertheless, the Board was able to reduce its fiscal year 2020 budget by 11% from a year earlier, to $57.6 million.

On July 31, the Board released its fiscal year 2019 annual report and sent it to the Governor of Puerto Rico, the Legislature, the U.S. Congress and the U.S. President, as required by PROMESA.[2]

IV. Fiscal Plan for the University of Puerto Rico

As I stated in my prior testimony, the University of Puerto Rico (UPR) is undeniably a center of academic excellence and a source of pride for all Puerto Ricans. There's probably not one person in Puerto Rico who would disagree with that statement. The Board believes that UPR is genuinely one of the best things that Puerto Rico has to offer. The Board remains committed to targeted measures to increase revenues and reduce expenditures essential to UPR operating sustainably and ensuring it remains at the center of Puerto Rico's successful economic development. The reforms are focused on maintaining the ability of all students to access and benefit from an improved university system.

As you will recall, the Government has been subsidizing UPR at a rate far exceeding the average for mainland U.S. states — roughly 70% instead of 20-30% — and at a time when it can no longer afford these subsidies in light of its own financial pressures. The UPR Fiscal Plan focused on creating savings by consolidating back-office functions across UPR's eleven campuses and improving procurement processes. Eleven campuses do not require eleven duplicative administrations. No cuts to faculty or student services are, or have ever been, planned, or are they necessary, if certain administrative savings and a new focus on improving revenues are implemented.

Revenues are depressed and insufficient at UPR due to extremely low tuition levels for all regardless of ability to pay, few "out of state" students, little success in attracting federal grants, and no active development of its superb alumni. The Fiscal Plan does require increased tuition but has ensured several safeguards to protect the most vulnerable. The maximum annual tuition ($5,090 in fiscal year 2023) will remain below current Federal Pell Grant award levels ($6,095), meaning all Pell Grant eligible students will be able to cover both tuition and some living expenses. The Fiscal Plan not only protects, but ensures funding of $280 million in needs-based scholarship funds over the Fiscal Plan period at both internal UPR and Commonwealth scholarship funds to guarantee that tuition increases never affect anyone who chooses to attend the UPR. If all these funds are disbursed each year (i.e. none of the external scholarship funds are converted to an endowment) they could provide the equivalent of over 12,000 full undergraduate scholarships (covering all tuition and fees) per year. Furthermore, after listening to the students of UPR, the

[2]See the Board's Fiscal Year 2019 Annual Report at: https://drive.google.com/file/d/19wcmgD-iYwi_JAsSGYWL_WK5kXJJggwV/view

Board increased the scholarship fund for students in need, so every Puerto Rican has access to the education they deserve. We have met with UPR administration numerous times and are willing to work with them to diversify UPR's sources of revenue.

Unfortunately, the UPR Administration recently announced that it is contributing less than half the actuarially required pension contribution to the UPR Retirement Plan ("UPRRP") for fiscal year 2020. This decision to undermine its pension obligations and to put the pensions of its faculty and staff at risk is grossly irresponsible, contrary to the Government's public policy of prioritizing pensions, and violative of PROMESA and the UPR Fiscal Plan certified by the Board in June.

According to the Board's recent actuarial analysis, if UPR makes no changes to its benefit structure or its funding policy, its pension plan could be insolvent by 2031, meaning that the UPRRP would not have sufficient funds to pay pension benefits after 2031. Rather than accepting that UPR may repeat the mistakes of ERS, JRS, and TRS at the Commonwealth, which became insolvent because their funding was far too low relative to the benefits they offered, the Fiscal Plan outlined three options that UPR could take to adequately fund the UPRRP, but each of the options requires UPR to make the full actuarially required contribution.

Instead of pursuing one of these options, UPR is knowingly defunding the UPRRP, putting the pensions of its faculty and staff at risk rather than heeding the advice of its actuaries, the Fiscal Plan, and the unfortunate experience from the Commonwealth. The Board will continue urging UPR to act to stave off its looming pension crisis. The first step is UPR making a determination about whether or not it wishes to reduce its required actuarial contribution in the future, in other words reforming its pension system. But, whatever UPR chooses, it must not put the UPRRP or pensions of faculty and staff at risk.

As stated in the UPR Fiscal Plan, the Board looks forward to partnering with UPR's stakeholders—including the Government of Puerto Rico, the UPR Governing Board, and the UPR Administration—in making the transition to a 'new status quo' operating model – one that is both more efficient and effective to bring the student and future generations of Puerto Rico the higher education that they deserved.

Although the path to implementing these reforms will not be easy, we want UPR to emerge a leaner and more effective academic institution among the best and most affordable in the United States and on the Island.

V. First Circuit Decision on the Unconstitutionality of the Board

As you know, on February 15, U.S. Court of Appeals for the First Circuit concluded that members of the Board are federal officials whose appointments must be made consistent with the Appointments Clause of the U.S. Constitution. Based on our belief that the members of the Board are territorial officers, not federal officers, and that the Appointments Clause does not apply to laws enacted pursuant to Congress's power under the Territories Clause, the Board filed a petition with the U.S. Supreme Court to review the decision by the First Circuit. The Supreme Court agreed to review the decision, and, at the Board's request, the First Circuit stayed its ruling pending the Supreme Court's final disposition of the case.

On April 29, 2019, President Donald J. Trump announced his intent to nominate the current members of the Board to undergo U.S. Senate confirmation to serve out the remainder of their terms. Those nominations have yet to be formally submitted to the Senate.

Last Tuesday, the Supreme Court heard oral arguments in the appeal, and we are expecting the Court's ruling in the coming months.

VI. PROMESA Discussion Draft

I appreciate the opportunity to now comment on aspects of the PROMESA discussion draft published by the Committee and the impact of those provisions on the work of the Board. The Board has serious concerns that several of these provisions, while well intended, will undermine the Board's pending negotiations and efforts to achieve a fair and expeditious resolution of claims consistent with the mandates of PROMESA and in the best interests of Puerto Rico and the people of Puerto Rico.

- **Section 4. Definition of Essential Public Services**

  This definition of essential public services specifies that public education, public safety, healthcare, and pensions are "essential public services," with the stated purpose to ensure their funding in the certified Fiscal Plan to the maximum extent possible. However, the Board believes that this provision could have the exact opposite effect, as it provides ammunition to those who have been arguing that the Board cannot fund services above and beyond their own highly restrictive interpretation as to what services are truly essential. The Board is facing this claim in the Title III cases. Creditors would welcome Congressional support for an essential service definition that could be used to advance their arguments. The result could be substantially reduced funding for services that the Board and the Government consider essential but that other parties convince the Court are not essential.

  As proposed, the definition in the discussion draft also provides for a minimum annual appropriation of $800 million to UPR. UPR's over-dependency on Central Government appropriations has led to its lack of commitment to generate its own revenue from out-of-state tuition, alumni donations, patent monetization and other means and its unwillingness to implement efficiencies. As previously noted, most U.S. universities receive 20-30 percent of their revenue from state government, whereas UPR received 70% from the Government in fiscal year 2018. The Board also considers any mandatory appropriations ill advised, as it does not and cannot take into consideration changes in circumstances, such as a significant increase in revenue from overseas students, a large increase in grant funding, or significant donations.

- **Section 6. Disclosure by Professional Persons Employed by Court Order**

  The Board supports the legislative proposal of Rep. Velázquez incorporated in the discussion draft to extend certain disclosure requirements from the Federal Rules of

Bankruptcy Procedure to professionals employed by the Board to avoid conflicts of interest and its goal of greater transparency and disclosure.

- **Section 7. Access to Information**

  The draft provides that any document, record, or information relating to the public debt of the Commonwealth of Puerto Rico is a public document and accessible to any interested party. Existing Puerto Rico disclosure laws adequately provide the public with rights to access to government documents. This provision overriding Puerto Rico law and making public any document relating to the negotiations or restructuring of the public debt would also be prejudicial and detrimental to the Board's effort to effectively and expeditiously secure the best deal possible for Puerto Rico and its people.

- **Section 8. Puerto Rico Infrastructure Revitalization Repealed**

  The Title V process has had some successes, most recently a generation facility for PREPA as noted above, but most private investment activity in recent years has been through the Puerto Rico P3 Authority, and those projects do not necessarily require the benefits of the Title V permitting process.

- **Section 9. Territorial Relief for Unsecured Public Debt**

  The discussion of a provision to allow Puerto Rico to cancel some of its unsecured debt may lead existing Puerto Rico General Obligation bondholders to demand secured debt in the current negotiations, which is more expensive and restrictive than unsecured debt. In effect, this provision could ultimately significantly reduce the amount of funding available to the Government to provide critical services to the people of Puerto Rico.

- **Section 10. Puerto Rico Public Credit Comprehensive Audit Commission**

  The Kobre & Kim independent debt investigation mentioned above effectively served the purpose of a debt audit. The Special Claims Committee is pursuing valid claims arising out of that report, and the Debt Management Policy in the Plan is designed to make sure these issues do not arise again.

- **Section 11. Office of Reconstruction Coordinator for Puerto Rico**

  The establishment of this office to manage and administer federal funds for the reconstruction of Puerto Rico as a result of Hurricane Maria could be helpful if it effectively served as a coordinator of the various federal agencies administering funding. Otherwise, the office risks becoming an unnecessary, additional level of bureaucracy further slowing down deployment of federal funds.

- **Section 12. Office of Revitalization Coordinator for Puerto Rico Electric Power Authority (PREPA)**

  The discussion of creating a revitalization coordinator for PREPA risks disrupting and undermining the transformation process of PREPA which is well underway. This process is being jointly run by the Board and Government and involves hiring a private operator to take over management of transmission and distribution as well as opening up generation for private investment and management.

The Board remains committed to working with the Chairman, the Ranking Member and Members of the Committee and the Congress as you continue oversight over implementation of PROMESA and consider any changes to the law.

VII. Federal Legislation Supporting Puerto Rico

Finally, the Board also continues to support legislative efforts of Chairman Grijalva, Ranking Member Bishop, Puerto Rico Resident Commissioner González-Colón, Representative Velázquez, Representative Soto, and many Members of this Committee and Congress to provide fairness for Puerto Rico in the distribution of federal funding and other federal programs essential to Puerto Rico and its people.

On behalf of the Board, I submitted a statement for the record in light of the Committee on Natural Resources' hearing on "The Insular Areas Medicaid Cliff" in support of equitable treatment for Puerto Rico in terms of the Medicaid program.[3] On June 19, I submitted a Statement to the House Ways and Means Committee in support of proposed legislation expanding the Earned Income Tax Credit to families in Puerto Rico.[4] On June 20, I submitted the Board's statement of support to Congresswoman Anna Eshoo, Chair, House Energy and Commerce Subcommittee on Health, again in favor of proposed legislation for more equitable distribution of Medicaid funding to Puerto Rico.[5]

The Board also continues to support the Government's request to receive equitable treatment in Medicare. Residents of Puerto Rico pay the same level of Medicare taxes as mainland residents, but the Island receives substantially lower payments in Medicare programs.[6]

VIII. Conclusion

In 2016, PROMESA – although not perfect – provided Puerto Rico with an opportunity to reset its reality. The compromise between both sides of the aisle to provide the Island with a novel mechanism to restructure its debt was certainly not easy to achieve. The leadership at the time of

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[3] See Executive Director Natalie A. Jaresko's Statement on this topic at: https://drive.google.com/file/d/1XeMmC0FCoq_S_uIdOR_JZU3FIO02Tmz-/view

[4] See Executive Director Natalie A. Jaresko's Statement on this topic at: https://drive.google.com/file/d/1EIjpHW-FVgdgVOYV_ftlwti5GiS2mCAo/view

[5] See Executive Director Natalie A. Jaresko's Statement on this topic at: https://drive.google.com/file/d/14PluCoX3012kDEY0CpZyDUgAkUl3k4CA/view

[6] A non-exhaustive list of legislation supported by the Board is available on page 80 of the Board's Fiscal Year 2019 Annual Report at: https://drive.google.com/file/d/19wcmgD-iYwi_JAsSGYWL_WK5kXJJggwV/view

PROMESA's adoption, and key figures such as Congresswoman Nydia Velázquez and Congressman Rob Bishop, fought hard to ensure Puerto Rico had a way out of its fiscal mess.

The Board strongly believes that the proposed draft text is a distraction from the real work already in process that we all need to do: to focus on getting the debt restructuring behind us and ensure the Government of Puerto Rico continues implementing the structural reforms, the fiscal responsibility, and better delivery of public services that the people of Puerto Rico deserve.

Massive debt is what caused Puerto Rico so much pain, and what is holding Puerto Rico's economic recovery back. That massive debt did not result in massively improved public safety, public health or public education. It takes a huge toll on the life of everyone who lives on this beautiful Island, and it is what denies us the stability Puerto Rico requires to rebuild its future and achieve prosperity.

The proposed Plan of Adjustment the Oversight Board filed is the beginning of a process that enables Puerto Rico to reach its real potential, where businesses large and small can have the confidence they need to invest and expand with certainty, and where the people of Puerto Rico can expect their government to provide safety, education and the public services the island needs. This is an important first step. We hope to continue our progress and to continue providing certainty that a better future lies ahead for Puerto Rico.

I concluded my May testimony with optimism and will conclude this one repeating it: Difficulties aside, I am optimistic and confident that we can and are all working together to ensure Puerto Rico's economic future is brighter than ever and that Congress finds confidence that Puerto Rico's problems can and will be solved.