



REVISED **FISCAL PLAN** FOR PUERTO RICO

2021-2022

AS SUBMITTED TO THE FINANCIAL
OVERSIGHT AND MANAGEMENT BOARD
FOR PUERTO RICO | MARCH 8, 2021

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- The short-term economic effects of COVID-19 on the global economy and the economies of the United States and Puerto Rico as they relate to Puerto Rico's tax revenue and budget.
- The longer-term economic ramifications of behavioral changes caused by COVID-19 (i.e., reduced travel, increased work from home, reduced activity in large gathering places, etc.).
- The amount of federal government aid provided to U.S. states and territories (including Puerto Rico) and the efficacy and speed of disbursement of such aid.
- The need to shift resources to create a more resilient structure to prevent or mitigate future pandemics.
- Any future actions taken or not taken by the United States federal government related to Medicaid.
- The amount and timing of receipt of any distributions from the Federal Emergency Management Agency (FEMA), U.S. Department of Housing and Urban Development (HUD)'s Community Development Block Grant-Disaster Recovery (CDBG-DR) Program and private insurance companies to repair damage caused by Hurricanes Irma and Maria and recent earthquakes in Puerto Rico.
- The amount and timing of receipt of any additional amounts appropriated by the United States federal government to address the funding gap described herein.
- The timeline for completion of the work being done by the Puerto Rico Electric Power Authority (PREPA) to repair PREPA's electric system and infrastructure and the impact of any future developments or issues related to PREPA's electric system and infrastructure on Puerto Rico's economic growth.
- The impact of the measures described herein on outmigration; and
- The timing and impact of the resolution of Puerto Rico's Title III cases and related litigation.

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List of Acronyms and Key Terms

AAFAF	Puerto Rico Fiscal Agency and Financial Advisory Authority (Spanish acronym)
ACA	Affordable Care Act
ADEA	Agricultural Enterprise Development Administration (Spanish acronym)
ADSEF	Family Socio-Economic Development Administration (Spanish acronym)
AFICA	Economic Development Bank; Industrial, Tourist, Education, Medical, and Environmental Control Facilities Financing Authority
AFSCME	American Federation of State, County and Municipal Employees
AMPR	Asociación de Maestros de Puerto Rico
April '18 Fiscal Plan	Fiscal Plan certified April 2018, immediately following Hurricanes Irma and Maria which first set out the major reforms
ASCE	American Society of Civil Engineers
ASEM	Puerto Rico Medical Services Administration (Spanish acronym)
ASES	Puerto Rico Health Insurance Administration (Spanish acronym)
ASG	General Services Administration (Spanish acronym)
ASSMCA	Mental Services Administration Health and Addiction (Spanish acronym)
ATM	Puerto Rico Maritime Transport Authority (Spanish acronym)
BBA	Bipartisan Budget Act
CAFR	Comprehensive Annual Financial Report
CAGR	Compound Annual Growth Rate
CAPEX	Capital Expenses
CARES	Coronavirus Aid, Relief, and Economic Security
CBO	Congressional Budget Office
CCDA	Convention Center District Authority
CDBG	Community Development Block Grant
CDBG – DR	Community Development Block Grant – Disaster Recovery
CDL	Community Disaster Loans
CELI	Contribution in Lieu of Taxes
CFO	Chief Financial Officer
CH	Correctional Health Department
CHIP	Children’s Health Insurance Program
CILT	Construction-in-lieu of taxes
COFIM	Municipal Finance Corporation (Spanish acronym)
COFINA	Puerto Rico Sales Tax Financing Corporation (Spanish acronym)
COR	Chief Operating Office
COR3	Central Office for Recovery, Reconstruction, and Resiliency
COSSEC	Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives (Spanish acronym)
COVID-19	Coronavirus Disease 2019
CPI-U	Consumer Price Index - Urban
CRIM	Municipal Revenue Collection Center
CRRSA	Coronavirus Response and Relief Supplemental Appropriations
CTC	Child Tax Credit
CUB	Clinton Utilities Board
DCR	Department of Corrections and Rehabilitation
DB	Defined Benefit pension plan
DC	Defined Contribution pension plan
DDEC	Puerto Rico Department of Economic Development Commerce (Spanish acronym)
DEC	Department of Environmental Conservation
DMO	Destination Marketing Organization
DMS	Data Management System
DOH	Department of Health
DOJ	Department of Justice
DOL-AO	Department of Labor Apprenticeship Office
DOS	Department of State
DPR	Discover Puerto Rico
DPS	Department of Public Safety
DRF	Disaster Relief Fund
DRS	Diagnosis Related Group
DSA	Debt Sustainability Analysis
EA	Environment Agency
E-FMAP	Enhanced Federal Medical Assistance Percentage
EHR	Electronic Health Record
EITC	Earned Income Tax Credit
ELL	English Language Learning
EMS	Emergency Medical Services
ER	Emergency Room
ERP	Enterprise Resource Planning
ERS	Employee Retirement System
FAM	Municipal Administration Fund
FDI	Foreign Direct Investment

Federal Government	The US Federal Government
FEMA	Federal Emergency Management Agency
FEMP	Federal Energy Management Program
FICA	Federal Insurance Contributions Act
FMAP	Federal Medical Assistance Percentage
FMM	Municipal Improvement Fund
FOMB	Financial Oversight and Management Board for Puerto Rico
FQHC	Federally Qualified Health Center
FTA	Federal Transit Authority
FTE	Full-Time Employee
FY	Fiscal Year
FYTD	Fiscal Year-To-Date
GAO	US Government Accountability Office
GDB	Government Development Bank for Puerto Rico
GDP	Gross Domestic Product
GF	General Fund
GFEWG	Governor's Fiscal and Economic Working Group
GHP	Government Health Plan
GNP	Gross National Product
Government	Government of Puerto Rico
Governor	Governor Pedro Rafael Pierluisi Urrutia
GSA	General Services Administration (also known as ASG)
Hacienda	Puerto Rico Department of Treasury
HHS	US Department of Health and Human Services
HIT	Health Insurance Tax
HIV	Human Immunodeficiency Virus
HR	Human Resources
HUD	US Department of Housing and Urban Development
Hurricanes	Hurricane Irma and Hurricane Maria
IDEAL	Electronic Identity Online Access System
IEP	Individualized Education Program
IFCU	Independently Forecasted Component Units
IMF	International Monetary Fund
INRIX	Software Company that manages traffic data
IoT	Internet of Things
IPR	Invest Puerto Rico
IRP	Integrated Resource Plan
IRS	Internal Revenue Service
Island	Puerto Rico
IT	Information Technology
JP	Junta Planificacion (Planning Board)
JRS	Judiciary Retirement System
K-12	Kindergarten through 12 th Grade
KPIs	Key Performance Indicators
LEA	Local Education Agency
LUMA	Electric Utility Company in Puerto Rico
March '17 Fiscal Plan	Fiscal Plan certified by the Financial Oversight and Management Board in March 2017, before Hurricanes Irma and Maria hit the Island
MADS	Maximum Annual Debt Service
MCOs	Managed Care Organizations
META-PR	Island's Standardized Tests
MEQC	Medicaid Eligibility Quality Control
MFCU	Medicaid Fraud Control Units
MICE	Meetings, Incentives, Conferences, and Exhibitions
MMIS	Medicaid Management Information System
MOU	Memoranda of Understanding
NAP	Nutrition Assistance Program (Spanish: Programa de Asistencia Nutricional, PAN)
NCQA	National Coalition for Quality Assurance
NGO	Non-Governmental Organization
NRW	Non-Resident Withholdings
O&M	Operations and Maintenance
OARTH	Office of Administration and Transformation of Human Resources (Spanish acronym)
OCFO	Office of the CFO
Oct '18 Fiscal Plan	Fiscal Plan certified by the Financial Oversight and Management Board in October 2018, updated for 2018 revenue and expenditure actuals
ODS	Office of Sustainable Development (Spanish acronym)
OECD	Organization for Economic Cooperation and Development
OGPe	Permits Management Office

OIPC	Office of Consumer Protection (Spanish acronym)
OMB	Office of Management and Budget
OPEB	Other Post-Employment Benefits
OPEX	Operating Expenses
ORES	Reorganization of Regional Offices
P3	Public Private Partnerships
P3 Authority	Public Private Partnership Authority
PA	Public Assistance
Parties	AAFAF and the Government
PayGo	Defined benefit actuarial responsibility program by which agencies and instrumentalities are responsible for paying their pensions obligations on an annual basis via a “PayGo Charge”
PB	Planning Board
PBA	Public Buildings Authority
PBL	Project Based Learning
PCOC	Consolidated Construction Permit
PDP	Parkinson’s Disease Psychosis
PDL	Prescription Drug List
PERM	Payment Error Rate Measurement
PFC	Public Finance Corporation
PISA	Program for International Student Assessment
Platino	Medicare Advantage program that also provides Medicaid wraparound services equivalent to Mi Salud / VITAL program
PMG	Primary Medical Group
PMO	Program Management Office
PMPM	Per Member Per Month
PRASA	Puerto Rico Aqueduct and Sewer Authority
PRCCDA	Puerto Rico Convention Center District Authority
PRDE	Puerto Rico Department of Education
PRDOH	Puerto Rico Department of Health
PREB	Puerto Rico Energy Bureau
PREMA	Puerto Rico Emergency Management Agency
PREMB	Puerto Rico Emergency Management Bureau
PREPA	Puerto Rico Electric and Power Authority
PRHFA (or HFA)	Puerto Rico Housing Finance Authority
PRHTA (or HTA)	Puerto Rico Highway and Transportation Authority
PRIDCO	Puerto Rico Industrial Development Company
PRITA	Puerto Rico Integrated Transit Authority
PRITS	Puerto Rico Information Technology Service
PROMESA	Puerto Rico Oversight, Management and Economic Stability Act
PRPB	Puerto Rico Police Bureau
PRTC	Puerto Rico Tourism Corporation
PSA	Plan Support Agreement
PSC	Puerto Rico Public Service Commission
PU	Single Business Permit
RESTART	Immediate Aid to Restart School Operations
RFP	Request for Proposal
RFQP	Request for Qualifications and Proposal
RIMS	Sustainable Improved Infrastructure Reconstruction
RR	Local Redevelopment Authority of Roosevelt Roads
SBP	Single Business Portal
SCO	State Coordinating Officer
SIFC	State Insurance Fund Corporation
SITA	System to track overtime hours
SNAP	Supplemental Nutritional Assistance Program
SPWD	Strategic Plan for Workforce Development
SRF	Special Revenue Fund
SR	Structural Reform
SRI	Permit
SSI	Supplemental Security Income
STEAM	Science, Technology, Engineering, Arts and Mathematics
STEM	Science, Technology, Engineering and Mathematics
SUT	Sales and Use Tax
T&D	Transmission and Distribution
TANF	Temporary Assistance for Needy Families
TRS	Teachers’ Retirement System
UPR	University of Puerto Rico
USDA	United States Department of Agriculture
USDC	United States District Court
VITAL	Medicaid Program in Puerto Rico
VTP	Voluntary Transition Programs

WDPO	Workforce Development Partnership Office
WIC	The Special Supplemental Nutrition Program for Women, Infants, and Children
WIOA	Workforce Innovation and Opportunity Act
WIPR	Puerto Rico Television Station
WTP	Workforce Training Program

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Executive Summary

The people of Puerto Rico need and deserve plentiful good jobs, a dynamic and prosperous economy, affordable and reliable electricity, and an efficient and responsive public sector. Since 2005, the number of people living under the poverty line has increased, the economy has shrunk, electricity has remained expensive and unreliable, the business environment has remained poor, and the public sector has provided declining levels of service.

On top of these longstanding economic challenges, multiple large-scale natural disasters have struck Puerto Rico in the last three years, testing the resiliency of economic and social institutions like never before.

In the fall of 2017, Hurricanes Irma and Maria inflicted unprecedented damage on the physical infrastructure of Puerto Rico, leaving large segments of the population without power for weeks and in many cases months. Thousands of Puerto Ricans died, many due to the after-effects of the storms rather than their direct impact. In the aftermath, the Island experienced widespread economic dislocation as the scale of the damage became evident. The negative impacts to housing, power and water infrastructure, and transportation infrastructure, created extremely challenging conditions for residents, while the small business sector especially suffered as a result of destroyed inventories and the abrupt negative shock to Puerto Rico's local economy.

After a very difficult period in the immediate aftermath of the storms, the economy gradually recovered, and efforts turned to rebuilding. Aided by a large-scale federal response, the hard work assessing the damage to critical infrastructure occurred through the fall of 2017 and into 2018.

Just as the Island was recovering from political disruption and embarking on reconstruction at the end of 2019, Puerto Rico suffered its most serious earthquakes in recent memory, resulting in structural damage to buildings across southwestern Puerto Rico. Residents of these communities also experienced hundreds of aftershocks over several months, some nearly as strong as the initial earthquakes. Public safety became a critical concern due to affect infrastructure, while businesses suffered further disruption and many schools, prisons, and other public buildings suffered severe damage. The full extent of the damage is still unknown and rebuilding efforts in some places have not yet begun.

Only two months after these major earthquakes, the COVID-19 pandemic brought Puerto Rico—and the rest of the world—to a standstill. Overnight, the economy shut down except for the most critical activities as the Government took prudent steps to mitigate the risk of a catastrophic public health crisis. Unemployment skyrocketed as many businesses were forced to close, while the local and federal governments quickly mobilized to provide support. Many initial projections indicated that the economic shock due to COVID-19 would be worse than that of the Great Recession. Fortunately, the combined economic impact of the federal and local fiscal stimulus measures and the gradual reopening of the national and local economies mitigated the negative shock and allowed certain of the Government's primary revenue sources to outperform the 2020 Certified Fiscal Plan projections.

The pathway to economic recovery remains highly dependent on the overall public health response, including the rate at which the population is vaccinated and the Federal Government's ability to provide economic support for those whose livelihoods are at risk. But more transmissible and potentially deadlier variants of COVID-19 are continuing to develop and spread, just as the rollout of vaccines had raised hopes for a broad-based economic recovery.

These new variants pose two threats to economic recovery. *First*, restrictions on activity could be extended or further tightened to counteract the higher risk of infection until a sufficient percentage of the population have been vaccinated, pushing some economies back into recession. *Second*, one or more of the new variants may become resistant to the immunity conferred by existing vaccines and past infections, potentially triggering a new cycle of restrictions and a new round of vaccinations. Much better infrastructure is needed to mitigate the ongoing COVID-19 threat, including: (i) more widespread genomic surveillance for dangerous variants; (ii) the capacity to quickly update and administer vaccines to the entire population; and (iii) widely available rapid testing to contain outbreaks.

Consistent with the Commonwealth's prior Fiscal Plans, the 2021 Fiscal Plan incorporates major structural reforms to restore competitiveness, enable growth and spur a return to prosperity, including (a) human capital, welfare, and education reforms to advance successful participation in the formal labor market; (b) reforms to streamline core business processes (e.g., paying taxes, registering property and obtaining permits) to improve the ease of doing business and enable job creation; and (c) proposals to enable reliable power and stable infrastructure for businesses and households. In addition to these structural reforms, the Fiscal Plans have focused on improving the responsiveness and efficiency of the Government, while reducing unnecessary administrative expenses and mitigating the escalating growth of healthcare costs.

At the onset of the COVID-19 crisis, the Government mobilized, in close partnership with the Oversight Board, to deliver immediate support and relief to the people of Puerto Rico. This effort included a \$787 million economic aid package to support frontline workers and small businesses. Then-Governor Vázquez also took executive actions that the Oversight Board supported to provide temporary relief on tax payment deadlines. Finally, the Oversight Board authorized a \$400 million advance on federal funding for economic impact payments administered by Hacienda, as well as a liquidity facility of up to \$185 million for municipalities suffering from revenue collection deferrals.

In spite of the Island's various natural disaster and public health emergencies since 2017, the Government has been able to drive meaningful progress in creating a leaner, more affordable government. As a result, the Government was able to: (i) increase expenditures during these times of crisis, while ensuring total expenditure levels remained within total available revenues; and (ii) avoid budget cuts that many U.S. states have been required to make as a result of COVID-19 related revenue declines.

In addition, Puerto Rico's unfair and inequitable treatment as an unincorporated territory has been a driving factor causing the Island's precipitous economic decline. Puerto Rico is treated unequally under key federal programs such as Medicaid compared to U.S. states. For example, the Census Bureau reported in 2014 that Oregon—a relatively prosperous state with a population size similar to Puerto Rico—received over \$29 billion from the Federal Government, whereas Puerto Rico received only \$19 billion for the same year. Puerto Rico's unequal treatment under federal economic assistance programs is also one of the primary causes of the severe income disparity between Puerto Rico and U.S. mainland residents. As a result of this disparate treatment, Puerto Rico residents have migrated to the U.S. mainland in unprecedented numbers, leaving Puerto Rico with a diminished workforce.

This 2021 Fiscal Plan represents the vision of Governor Pierluisi's administration for the future of Puerto Rico. The Fiscal Plan assumes that Puerto Rico will, consistent with President Biden's commitment for providing Puerto Rico parity in Federal Funding Programs, receive state-like treatment for purposes of obtaining Medicaid federal funding which represents an ~83% federal matching level for its largest Medicaid population. The additional general fund budget that is available on account of the incremental federal Medicaid dollars is assumed to be used to (i) provide all the needed benefits to improve the coverage and affordability of the health system (such as the long-term care and Medicaid premium and cost-share) (ii) to fund the

Governor's initiatives (such as Uniform Remuneration, No more cuts to the UPR and Municipalities, etc.), (iii) and to adjust corporate and personal income taxes to a level that is more in line with other U.S. jurisdictions, thereby improving the business environment and competitiveness of Puerto Rico. Moreover, the 2021 Fiscal Plan continues to include actions that will be taken to make structural reforms to the economy, improving labor force participation, the ease of doing business and energy and infrastructure management. The Fiscal Plan includes dozens of initiatives that the Government will take to create a more accountable and transparent government, with resources focused on improving the front-line services that matter. The 2021 Fiscal Plan includes the following initiatives that will be a focus of Governor Pierluisi's administration:

- No further decrease in UPR appropriations.
- No further decrease in Municipal appropriations.
- Defend pensions by seeking adequate funding to protect the benefits for the Island's most vulnerable pensioners, among other measures.
- Incorporation of the uniform remuneration plan, parametric insurance program, and other miscellaneous initiatives to improve Puerto Rico.
- Provide an exemption to municipalities from having to contribute to Puerto Rico's Medicaid program.

Defending public sector pensioners is a central pillar of the Government's public policy. Public pensioners have already suffered enough over the last decade, having had their benefits reduced through prior concessions.

While the Government is steadfast in its continued and unwavering commitment to the defense of pensioners, it is cognizant of the Oversight Board's continued attempt to institute certain pension reforms (including cuts and benefit freezes at TRS and JRS). In the face of these Oversight Board efforts, the Government will take all steps to mitigate the potential legal risks to pension payments that will arise in the Commonwealth's Title III proceedings. In that regard, the Government will prioritize budgetary support of pensioners, even in the face of court-imposed pension cuts or the freezing of benefit accruals, in order to ameliorate the harsh effects of aggressive pension cuts.

The Government will use the newly established Benefit Restoration Mechanism and the Pension Reserve Trust to support the affected pensioners to the maximum extent possible. Moreover, if necessary, the Government will prioritize required budgetary allocations to provide adequate funding to cushion and offset any pension cuts. The Government will continue to seek additional sources of funding for any pension cuts as may be imposed by the Oversight Board and Title III Court in the Commonwealth's Title III proceeding.

* * *

Prior to the enactment of PROMESA, Puerto Rico had been mired in an economic and demographic decline for a decade. As of 2019, the economy contracted by 20% in real terms¹ and the population is roughly 16% lower² (largely due to outmigration) than it was in 2005 – trends that, even before recent natural disasters, were projected to continue. Over 43% of the population (including ~58% of Puerto Rican children) lives below the poverty line, ~47%

¹ Reflects Gross Product in Constant 1954 Dollars. DevTech Systems MAPSS, Reports for the Governor of Puerto Rico, 1965-2019.

² Selected Demographic Statistics, DevTech System MAPSS, Reports for the Governor of Puerto Rico, 1965-2019.

are dependent on Medicaid for healthcare, and the median household income is \$20,539, less than one-third of to the U.S. average of \$68,703.

Before PROMESA, the consolidated Commonwealth's outstanding debt and pension liabilities grew to over \$120 billion—an amount that is almost twice the size of Puerto Rico's economy and includes more than \$70 billion in financial debt and more than \$50 billion in pension liabilities.

These core challenges were not new and temporary; they had been long-standing and structural. For decades, the private sector was overly reliant on now-expired federal tax advantages while operating in a difficult business climate with poor infrastructure, cumbersome laws and regulations, and expensive and unreliable electricity and transit systems.

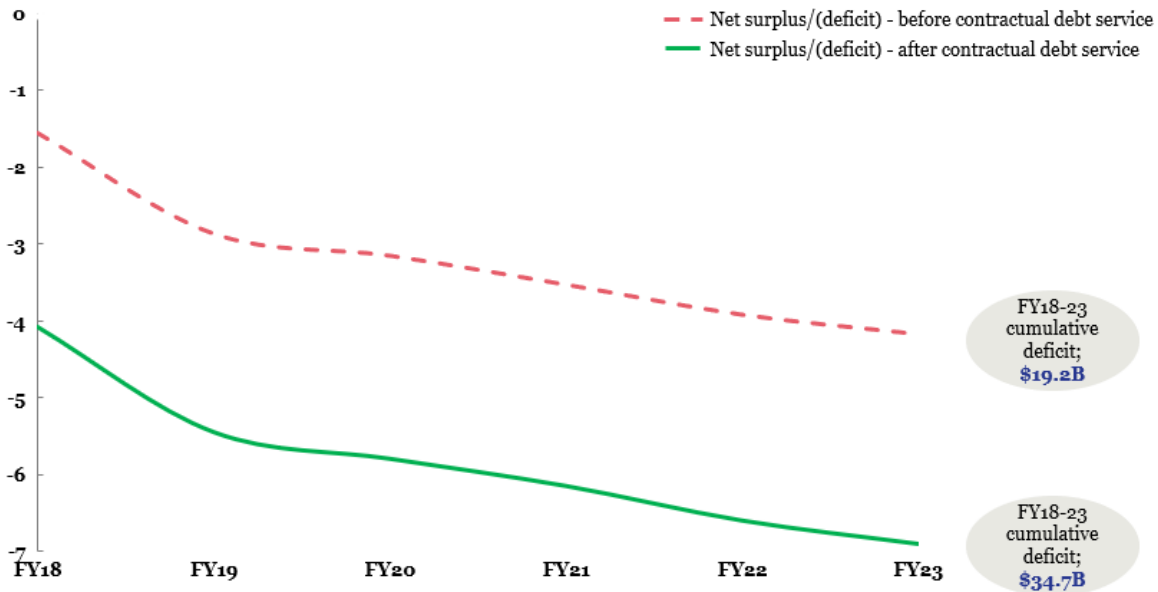
Other challenges included a large public sector that struggled to deliver improved outcomes in critical areas such as ease of doing business and education, while maintaining a labor force participation rate that was (and continues to be) among the lowest in the world. In the World Bank's Worldwide Governance Indicators, Puerto Rico ranks far below the mainland United States in "voice and accountability" for residents, government quality, regulatory quality, rule of law, and control of corruption.³ In the OECD's 2015 Program for International Student Assessment (PISA), only six countries or regions in the world scored lower than Puerto Rico in science and reading, and only three scored lower than Puerto Rico in math.⁴ In 2019, Puerto Rico had 73,000 less public employees than in 2010, a decline of over 26% of public sector headcount. The downsizing reflected revenue pressures and led to further challenges to services delivery. Likewise, of the 233 countries or regions for which the World Bank measures labor force participation rates, Puerto Rico is currently ranked 232. In the three decades that the World Bank has gathered such data, Puerto Rico has never ranked higher than 212.

Puerto Rico has had fiscal management challenges for years, which contributed to an ever-growing deficit. This deficit was difficult to forecast with certainty because of protracted delays in issuing annual audited financial statements, lack of proper fiscal controls, lack of centralized financial records and inefficient financial management. Puerto Rico also has been in an economic decline for over a decade, which (in addition to ongoing outmigration) has eroded the Government's tax base. To finance these primary deficits, Puerto Rico historically resorted to issuing debt that eventually became unsustainable. When Congress enacted PROMESA in 2016, the Commonwealth was projected to run structural annual deficits exceeding \$7 billion, or \$3 billion before debt service.

³ The World Bank Group, Worldwide Governance Indicators.

⁴ U.S. Department of Education, Institute of Education Sciences, National Center for Education Statistics, Program for International Student Assessment (PISA) 2015, State Results: Puerto Rico.

EXHIBIT 1: PROJECTED PRE-FISCAL PLAN DEFICIT - BEFORE THE HURRICANES (\$B)



* * *

In light of Puerto Rico’s economic crisis and the Government’s unsustainable financial path, the Government and Oversight Board have set out to find long-term solutions, even if not always agreeing on the same approach, as outlined below:

- **Creating a leaner, more affordable government.** The Oversight Board has outlined necessary changes to streamline Government operations and reduce unnecessary administrative expenses. Such reforms include improving the management of public education; pursuing civilianization to enable more sworn police officers to move into the field; consolidating agencies to enable coordination and back-office efficiencies, reducing the correctional system footprint to enhance staffing practices; and incorporating best practices in digitization.
- **Identifying specific actions needed to reform the structure of the economy and create the conditions for growth in Puerto Rico.** The Oversight Board and the Government have developed a comprehensive plan to drive economic growth by improving participation in the formal labor market: spurring job creation, transforming the education system, improving access to reliable infrastructure and energy, and supporting the people of Puerto Rico through workforce development programs.
- **Increasing transparency of and controls over Government finances.** The Oversight Board and the Government have: (a) improved the budgeting process; (b) established regular reporting on cash and actual expenditures; (c) adopted formal processes for reappropriations and allocation of capital expenditures; and (d) conducted reviews of major contracts to ensure fiscal plan compliance. As a result of these efforts, Puerto Rico’s stakeholders have been given a common set of facts about the Government’s current fiscal situation, which has reduced superfluous and non-transparent spending.

- **Directing resources to front line service delivery.** The Government and Oversight Board have enhanced the impact of Government spending through: (i) priority investments in areas of demonstrated need such as public safety, health care, education; and (ii) improved natural disaster response.
- **Maximizing the impact of federal investments in Puerto Rico.** The Government and Oversight Board have placed particular emphasis on aligning federal funds towards investments that will accelerate progress as much as possible within key reform areas such as: infrastructure, COVID-19 response, health system improvements, educational outcomes, and economic growth.

* * *

Puerto Rico can overcome this current public health and economic crisis. It will be a difficult road ahead over the coming months and years, but the people of Puerto Rico have proven their resiliency.

Puerto Rico will continue the pursuit of bold actions to improve its fiscal and economic trajectory. The Island's economic future is more uncertain than ever due to the damaging effects of two catastrophic hurricanes, unprecedented earthquakes, and a devastating global pandemic. Nevertheless, Governor Pierluisi's administration has a comprehensive plan (as described in this 2021 Fiscal Plan) to create the best possible conditions for Puerto Rico's economic recovery, which will inure to the benefit of its people and businesses and provide for a Government that is more effective and responsive to its residents.

Government efficiency and other fiscal measures

The 2021 Fiscal Plan includes various efficiency measures that the Government plans to continue to make it more responsive and effective:

- **Agency efficiencies:** Streamlining agencies to leverage valuable human and financial resources, further centralizing procurement to achieve greater purchasing power and transparency, transforming processes, and deploying new management tools and practices to deliver better governmental services for substantially lower cost.
- **Creation of Office of the CFO:** Instituting fiscal controls and accountability, centralizing fiscal authority, and improving governance, accountability, and transparency over budgets, reform implementation, procurement, and personnel.
- **Medicaid reform:** Taking the necessary steps to curb fraud, waste and abuse in the healthcare system.
- **Enhanced tax compliance and optimized taxes and fees:** Employing new technology and other innovative and commonly used practices in other jurisdictions to broaden the tax base, reduce fraud, and improve fairness to boost overall tax revenues, and adjusting existing taxes and fees to capture revenues from under-leveraged sources. The 2021 Fiscal Plan assumes that all revenue measures have been achieved by the end of FY2021 and are included as part of the baseline revenue projections.

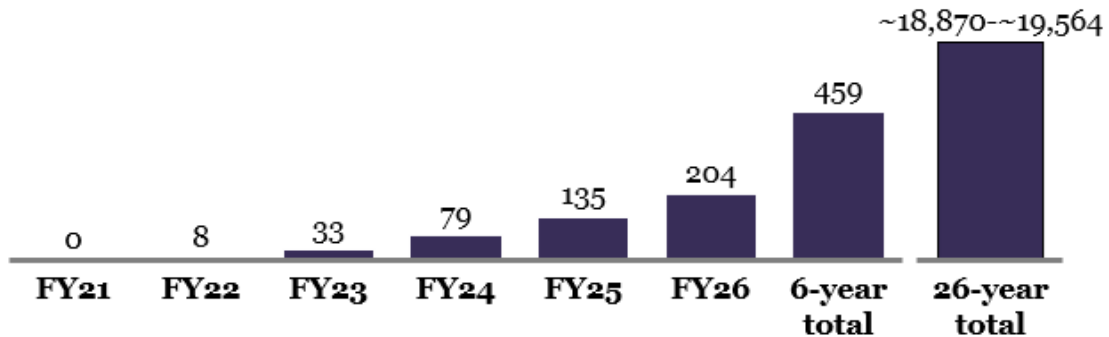
The majority of the revenue and expense measures which were first introduced in 2018 have been implemented to date by the Government and are included in the baseline expenses as part of the FY2021 and FY2022 budget.

Structural reforms

The 2021 Fiscal Plan includes the following structural reforms:

- **Human capital and welfare reform:** Promoting participation in the formal labor force by creating incentives to work through Earned Income Tax Credit (EITC)⁵ benefits and Nutritional Assistance Program (NAP) reform, as well as providing comprehensive workforce development opportunities. EITC and NAP reform are projected to increase the economic growth rate by 0.15% in FY2026.
- **K-12 education reform:** Transforming the K-12 education system to dramatically improve student outcomes and contribute to an effective workforce in the long-term. Education reforms are projected to add 0.10% to GNP growth rate by FY2046.
- **Ease of doing business reform:** Improving the competitiveness and attractiveness of Puerto Rico’s economy by (i) reducing obstacles to starting and sustaining a business through improvements to the processes for obtaining permits, registering property, and paying taxes; and (ii) establishing best-in-class entities to attract investment and increase tourism. These reforms are projected to drive a 0.30% uptick in overall growth by FY2025.
- **Power sector reform:** Providing affordable and more reliable energy through the transformation of PREPA, the establishment of an independent, expert, and well-funded energy regulator, and the development of cleaner and lower cost power generation. This reform is projected to increase growth by 0.30% by FY2024.
- **Infrastructure reform:** Integrating all appropriate transit assets under PRITA, so it can act as a unitary transit authority managing all relevant transit assets on the Island (e.g., all buses, ferries, and Tren Urbano), and reforming the public transportation sector more broadly.

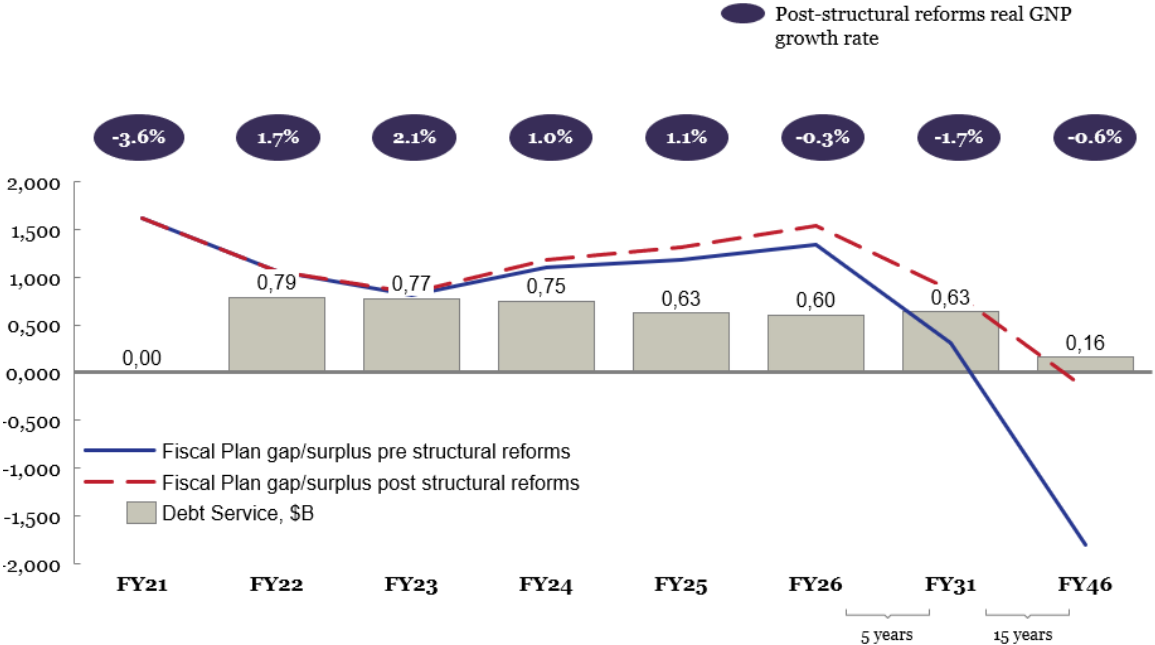
EXHIBIT 2: IMPACT OF STRUCTURAL REFORMS (\$M)



Implementing these structural reforms will enable the Island to move closer to a reality in which it has low-cost and reliable energy, robust infrastructure, more incentives to enter the formal labor market, an improved regulatory and permitting environment, and a more effective and efficient public sector, as outlined in Exhibit 3 below.

⁵ Legislation pending approval before Congress.

EXHIBIT 3: 2021 FISCAL PLAN ANNUAL PROJECTED SURPLUS BEFORE AND AFTER STRUCTURAL REFORMS (\$M)



¹ Contractual debt service does not include COFINA debt service. Reflects debt service per the February 2021 plan support agreement term sheet. Pre- and Post- structural reforms surplus exclude debt service, which is illustrated separately.

PART I: Context for Puerto Rico's Current Economic and Fiscal Challenges

Chapter 1. Long-term economic trends in Puerto Rico

Even before suffering a series of natural disasters in the form of hurricanes, earthquakes, and the COVID-19 pandemic from 2017-2020, Puerto Rico's economy had been in an acute structural decline for over a decade. The Government had defaulted on much of its debt, and nearly half of Puerto Ricans lived below the national poverty line. The reasons for these problems are multiple, but the root causes stretch back 40 years.

In the 1940s and 1950s, Puerto Rico's economy grew rapidly with productivity increasing by 5% per annum as the Island transitioned from an agricultural-led to a manufacturing-led economy. However, as economic performance began to decline in the 1970s, the Federal Government adopted two significant policies to help Puerto Rico shore up its economy.

First, transfer programs increased dramatically, particularly as Puerto Rico started receiving Nutritional Assistance Program (NAP) funding, which eventually provided (in aggregate) a proportion of residents' personal income that was twice the U.S. mainland average. In addition to raising costs for the Government, at times these programs created disincentives to work—due to benefits that were high relative to wages available in the formal labor market.

Second, in 1976, Congress enacted Section 936 of the U.S. Internal Revenue Code to promote corporate investment by allowing companies to transfer their “intangible assets” to Puerto Rico, thereby shifting profits to the Island. These Section 936 companies were primarily in the pharmaceutical and life-sciences sectors and became a pillar of Puerto Rico's economy, creating valuable local supply chains and local banking deposits while contributing substantial tax revenue. That same year, the Government passed Law 80 to protect Puerto Rican workers from wrongful discharge by, among other things, mandating severance for firms attempting to remove employees.

In 1996, Congress decided to end Section 936, gradually phasing it out by 2006. During the same time, the Government, in response to an anemic local private sector, was expanding Government employment opportunities to the point that, by 2000, 30% of Puerto Rico's jobs were in the Government and 40% of workers with college degrees worked in the public sector. Major sectors such as water, electricity, and ports are still run by public corporations, and have consistently drained the economy by delivering lower quality services at higher costs, while crowding out private investment. There was also pervasive cross-subsidization among the Government, its public corporations, and other parts of the public sector that obfuscated financial management and accountability. In addition, a high degree of political interference in operational decision-making caused Puerto Rico to underperform on all important measures of a modern economy, including educational attainment, electricity cost, water quality, tax compliance, and labor market participation.

When the Great Recession hit in 2008, Puerto Rico's economy was already in a fragile fiscal and financial position. Since then, the economy has continued to deteriorate. Puerto Rico's GNP has

receded by 17%, labor force participation fell to a record low of 41%, and population decline by 15%.⁶ Puerto Rico is much poorer today relative to the mainland U.S. than it was in 1970.

⁶ GNP and population decline represent the change between 2008 and 2018 per data from the World Bank Group's World Development Indicators.

Chapter 2. Enactment of PROMESA, Commencement of Title III Cases, and Restructuring Progress

By 2016, Puerto Rico had accumulated over \$50 billion in unfunded pension liabilities and over \$70 billion of debt and was facing an imminent default. Because Puerto Rico and its public corporations cannot take advantage of Chapter 9 of the US Bankruptcy Code and an attempt to create a territorial bankruptcy law was struck down by the US Supreme Court; Congress stepped in to head off Puerto Rico's financial and debt crisis by passing the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA). PROMESA imposed an automatic stay on Puerto Rico's debt obligations and created the Financial Oversight and Management Board for Puerto Rico (the "FOMB" or "Oversight Board"). The Oversight Board is tasked with restructuring Puerto Rico's staggering debt burden and restoring sustained economic growth to Puerto Rico so that the Government can achieve fiscal balance and regain access to the capital markets.

Immediately after its formation, the Oversight Board began working with the Government to create a fiscal plan designed to achieve fiscal responsibility and access to the capital markets. The initial outcome of this work was the Commonwealth Fiscal Plan that the Oversight Board certified on March 13, 2017 (the March 2017 Fiscal Plan). A few months later, the Oversight Board commenced Title III cases for the Commonwealth, COFINA, HTA, ERS, and PREPA, thereby imposing an automatic stay on the enforcement of debt obligations of these entities. On September 27, 2019, the Oversight Board also commenced a Title III case for PBA.

Over the last four years, the Government has worked with the Oversight Board to make substantial progress in its PROMESA Title III cases and related restructurings, including the following key milestones:

- **November 2018:** On November 28, 2018, the Government completed a Qualifying Modification for GDB under Title VI of PROMESA, which restructured approximately \$4.7 billion of certain bond and deposit claims against GDB by exchanging those claims for \$2.6 billion of new bonds issued by a newly created public instrumentality—the GDB Debt Recovery Authority—and GDB transferred to such entity its municipal loan portfolio, a portion of its public entity loan portfolio, its real estate owned assets and its unencumbered cash. Through its Qualifying Modification, GDB achieved approximately \$2.1 billion of savings.
- **February 2019:** Three months later, on February 12, 2019, the Title III plan of adjustment for COFINA became effective, which reduced COFINA's bond debt from approximately \$17.6 billion to \$12 billion through a bond exchange and resolved the allocation of SUT revenues between the Commonwealth and COFINA. Through its Title III plan of adjustment, COFINA achieved approximately \$5.6 billion of savings.
- **June 2019:** On June 7, 2019, the Oversight Board and the Retiree Committee entered into a plan support agreement (the Retiree Committee PSA), providing for the Retiree Committee's support for the terms of a plan of adjustment that would include: (a) reducing monthly pension benefits in excess of \$1,500 per month by 8.5%, provided that the individual's total monthly benefit cannot fall below \$1,500 per month; and (b) establishing a pension reserve fund to provide a guaranteed source of payment in years when the annual budget falls into deficit. The Pierluisi administration's position on these pension cuts is that they are neither necessary nor proper and continue to defend the pensions in connection with any Title III plan of adjustment.

- **September 2019:** On September 27, 2019, the Oversight Board filed the initial joint plan of adjustment for the Commonwealth, ERS, and PBA, which reflected the terms of the Retiree Committee PSA.
- **February 2020:** The Oversight Board and creditors continued to engage in mediation after the filing of the initial joint plan of adjustment. As a result, on February 9, 2020, the Oversight Board announced the execution of a Plan Support Agreement (the February 2020 PSA), which had the support of approximately \$10 billion of GO and PBA Creditors. On February 28, 2020, the Oversight Board filed a revised plan of adjustment for the Commonwealth, ERS, and PBA to reflect the terms of the February 2020 PSA (the 2020 Plan Proposal).
- **March 2020:** Only two weeks after submitting the 2020 Plan Proposal, the global spread of COVID-19 caused a nationwide economic shut down that has had substantial negative effects on the people and businesses in Puerto Rico. As a result of the Island’s uncertain post-COVID-19 economic reality, the Oversight Board decided to pause discussion and prosecution of the 2020 Plan Proposal and sought to re-evaluate the February 2020 PSA. Accordingly, on March 23, 2020, the Oversight Board filed a motion requesting the disclosure statement hearing for the 2020 Plan Proposal be adjourned.
- **August 2020:** The Oversight Board re-engaged with creditors through the mediation process to discuss adjustments to the February 2020 PSA in an effort to come to an agreement with a similar group of GO and PBA bondholders. These parties were unable to reach an agreement at that time.
- **October 2020:** On October 6, 2020, the PSA Creditors filed a motion to impose certain deadlines on the Oversight Board to prosecute or modify the 2020 Plan Proposal. Moreover, the PSA Creditors argued that the Title III Cases should be dismissed if the Oversight Board did not meet the PSA Creditors’ proposed deadlines. The Government objected to the PSA Creditors’ motion, noting that the unrealistic timeline the PSA Creditors proposed ignored the setbacks and realities forced upon Puerto Rico due to the ongoing COVID-19 crisis and, if such deadlines were imposed, they would severely undermine the Government’s ability to carry out its obligation to protect its people. The Government also argued that dismissal of the Title III Case would end PROMESA’s litigation stay and unleash another round of piecemeal litigation (similar to what Puerto Rico and its people experienced prior to 2017) and would do nothing to advance a restructuring or repayment of debt. On October 29, 2020, the Title III Court entered a Plan Scheduling Order, directing the Oversight Board to file a revised term sheet on or before February 10, 2021. The order instructed that the Oversight Board file “an informative motion presenting a term sheet disclosing the material economic and structural features of an amended plan of adjustment that the Oversight Board intends to propose for confirmation, and a motion for approval of a proposed timetable for the filing of an amended plan and proposed disclosure statement (if one has not yet been filed), discovery and litigation in connection with such proposal, solicitation, voting, and confirmation proceedings.”
- **November 2020:** Following the direction from the Title III Court, the Oversight Board resumed negotiations with GO and PBA bondholders, as well as other creditor groups, pursuant to the mediation agreement on November 20, 2020.
- **December 2020:** Mediation resumed the first week of December 2020, with Government participation.
- **February 2021:** On February 9, 2021, the Oversight Board and the principal parties to the February 2020 PSA reached an agreement in principle regarding the terms of an amended plan of adjustment, subject to the execution of definitive documentation, including, without limitation, the execution of a plan support agreement. On February 23, 2021, the Oversight

Board announced the termination of the 2020 PSA and execution of a new plan support agreement, dated February 22, 2021 (the February 2021 PSA). The February 2021 PSA has garnered the support of over 70% of holders of GO Bonds and PBA Bonds but has not yet received support from certain other remaining creditor groups. In connection with the Oversight Board's announcement on February 9, 2021, the Government noted it believes a workable economic framework has been achieved, although it has communicated to the Oversight Board that the Government continues to believe in (and will only support) a plan of adjustment without cuts to pension and retiree benefits.

On February 16, 2021, the Title III Court entered an order amending its October 2020 Plan Scheduling Order to extend the Oversight Board's deadline to file an amended plan of adjustment to March 8, 2021. The Government has not yet determined whether it will support the February 2021 PSA, or any amended plan of adjustment given its view that Government pensioners must be protected and must not receive additional cuts to their pension benefits.

Chapter 3. Fiscal plan updates due to natural disasters and emergencies

Over the last four years, the people of Puerto Rico have endured a series of natural disasters and emergencies without precedent in modern history. As a result of these events, the Oversight Board has certified revised Commonwealth fiscal plans to reflect their impact of Puerto Rico's economy and fiscal projections.

On September 6, 2017 and September 20, 2017, respectively, Hurricanes Irma and Maria struck Puerto Rico, causing unprecedented humanitarian, economic, and infrastructure-related damages and upending the daily lives of Puerto Rico's over three million residents. Thousands of residents were left homeless, basic utilities were completely shut down, and schools, hospitals, and businesses were destroyed. Tens of thousands of Puerto Ricans fled the Island. The Federal Government's response has become one of the largest and most complex disaster recovery efforts in U.S. history.

The damage inflicted on Puerto Rico by the Hurricanes required the March 2017 Fiscal Plan to be revised. Therefore, on October 31, 2017, the Oversight Board formally requested that the Government submit a revised Fiscal Plan for the Commonwealth and its instrumentalities based on Puerto Rico's new post-hurricane economic reality. After months of hard work, engagement with stakeholders, and intense negotiations with the Government, the Oversight Board certified its own Fiscal Plan for the Commonwealth on April 19, 2018, which was subsequently amended and recertified on May 30, 2018 and June 29, 2018 (the June 29, 2018 Certified Fiscal Plan). This Fiscal Plan reflected Puerto Rico's post-hurricane economic environment and implemented incremental structural reforms focused on improving the competitiveness of the local labor market.

On August 1, 2018, the Oversight Board requested the Government submit a further revised fiscal plan to replace the June 29, 2018 Certified Fiscal Plan in light of new information including, among other things, fiscal year 2018 financial information, revised federal disaster spending estimates, and updated demographic projections. After several months of discussions and Government proposals, the Oversight Board eventually certified its own revised Fiscal Plan for the Commonwealth on October 23, 2018, which was subsequently updated and recertified on May 9, 2019.

On December 28, 2019, the first of many significant earthquakes shook Puerto Rico, registering at a magnitude of 4.7 on the Richter scale. On January 6, 2020, Puerto Rico experienced a 5.8 magnitude earthquake. The next day, Puerto Rico experienced a magnitude 6.4 earthquake, its strongest and most destructive earthquake in a century. That same day, the Oversight Board approved the Government’s request to access funding from its Emergency Reserve for FY2019 and FY2020 (\$260 million in total) to bolster the response to the earthquakes. On May 2, 2020, an earthquake with a 5.4 magnitude struck Puerto Rico’s southwestern coast. The seismic event, which briefly knocked out power in some areas, hit near the city of Ponce. These earthquakes represent only four of more than 1,000 overall earthquakes of magnitude 3 or greater in Puerto Rico during 2020, with six over a magnitude 5.5. Hundreds of structures—including homes, local government institutions, small businesses, and houses of worship—have been damaged or destroyed by these devastating shocks. According to a January 29, 2020 report, published by the United States Geological Survey (USGS), there is a high likelihood of continued, material aftershocks over the course of the next several years.⁷ While there likely will be fewer earthquakes over time, Puerto Rico continues to be at risk of potentially catastrophic earthquakes.

On top of the hurricanes and earthquakes, Puerto Rico—like the rest of the world—was confronted with the global COVID-19 pandemic in early 2020, which has required immediate action and persistent vigilance.

On March 3, 2020, the Oversight Board made available emergency reserve funds for use in preparedness and response activities related to COVID-19. In so doing, the Oversight Board supported the Government’s efforts to act quickly and limit the risk to the people of Puerto Rico to the maximum extent possible. On March 15, 2020, Governor Vázquez signed Executive Order 2020-023, which directed the “closure of all businesses in Puerto Rico as of March 15 at 6:00 p.m.” for two weeks, putting Puerto Rico into lockdown earlier than any U.S. state. The Executive Order also imposed a curfew from 9:00 p.m. through 5:00 a.m. during which time all residents of Puerto Rico were to remain in their residences. However, only businesses related to the distribution of food, medical supplies and equipment, gas, financial and banking institutions, and elderly care centers were excluded and remained open. In addition, the Government closed San Juan Bay to cruise ship vessels effective as of March 17, 2020. On March 30, 2020, Governor Vázquez announced that, based on recommendations from the Government’s Health Taskforce and the continuing state of emergency, the curfew and business closures established in the Executive Order were extended until April 12, 2020. Further executive orders have subsequently extended these measures, with modified curfew periods and scope of business closures to reflect the ongoing and ever-changing nature of the COVID-19 crisis.

The effects of the current public health crisis have been far-reaching and devastating, both as a humanitarian crisis and economically. To provide additional support to the Island in responding to the COVID-19 pandemic, the Government initiated the FY2020 Emergency Measures Support Package budget, which the Oversight Board certified on April 2, 2020. This \$787 million budgetary allocation provided the Government critical resources necessary to respond to the significant difficulties arising from the Emergency Measures instituted to contain and mitigate COVID-19. More specifically, it provided direct financial support payments to self-employed individuals and small businesses, bonuses for frontline workers, funds for medical supplies, support to municipalities, and resources for PRDE to purchase equipment to facilitate distance learning.

Governor Vázquez issued additional executive orders in response to COVID-19 to issue a state of emergency due to the pandemic and to address, among other things, (i) homelessness, (ii) school and private sector closures, (iii) the acquisition of goods and services, (iv) use of the National Guard, (v) prompt diagnosis of COVID-19 through widespread testing and other measures,

⁷ U.S. Geological Survey, 2020 Southwest Puerto Rico Earthquake Sequence (January 29, 2020).

(vi) special leave for public employees affected by COVID-19, (vii) and the creation of a medical task force to advise the Governor on COVID-19 response efforts. Taken together, these measures intended to protect the physical, mental, and economic health of the people of Puerto Rico, while preserving the social fabric of the Island's diverse communities.

In light of the substantial impacts of the 2020 earthquakes and COVID-19 pandemic, the Oversight Board requested the Government to submit a new fiscal plan to replace the then-operative May 9, 2019 Certified Fiscal Plan. After several Government submissions and discussions with the Oversight Board, the Oversight Board certified its most recent Fiscal Plan for the Commonwealth on May 27, 2020.

As with prior Fiscal Plans, the 2021 Fiscal Plan includes updates with new information about Government revenues and expenditures based on observed trends and new information coming to light in the past year. Additionally, the 2021 Fiscal Plan includes a revised forecast of Puerto Rico's macroeconomic outlook based on recent events and performance, as outlined in *Chapter 4*.

PART II. Puerto Rico's Path to Fiscal and Economic Sustainability

Chapter 4. Macroeconomic and demographic trajectory

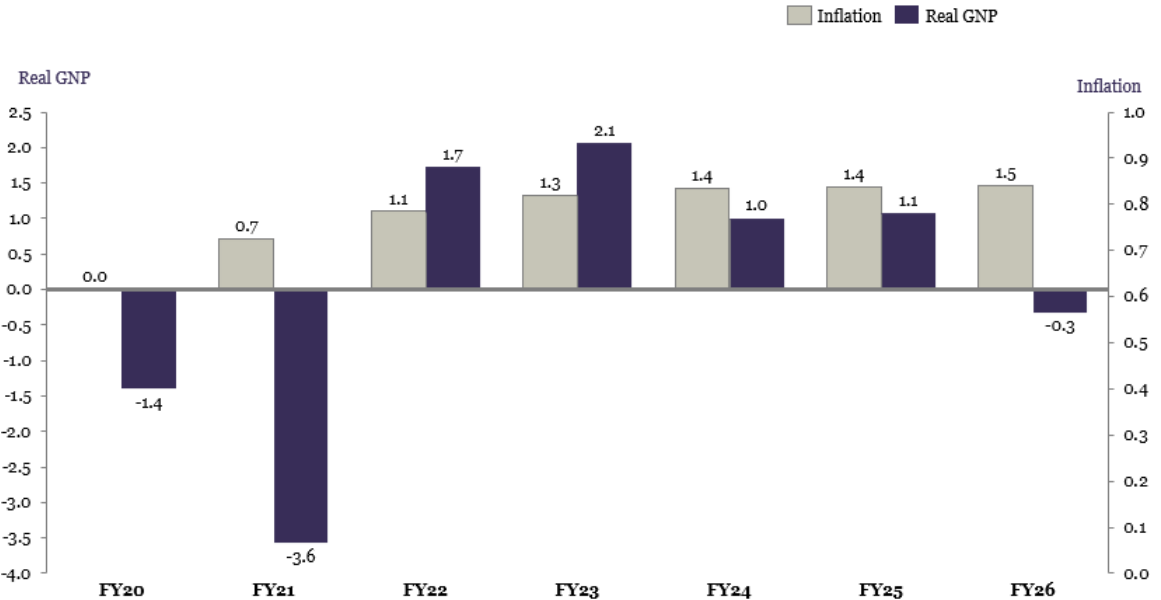
The 2021 Fiscal Plan estimates that the economy of Puerto Rico declined by 1.4% in real terms in FY2020 and is expected to continue to decline an additional 3.6% in FY2021. These estimates reflect a series of pandemic related policies and that were unknown at the time of writing the May 27, 2020 Certified Fiscal Plan, which forecast a 4.0% decline in Puerto Rico Real GNP in FY2020. Upward revisions reflect a confluence of developments that have materialized to increase support in the economy, as outlined below:

- **A stronger starting point for the U.S. mainland economic forecast.** Multiple vaccine approvals and the launch of vaccination have raised hopes of an eventual end to the COVID-19 pandemic. Economic data for the mainland suggest stronger-than-projected momentum, on average, across regions in the second half of calendar year 2020, with economic activity adapting to subdued contact-intensive activity with the passage of time. Moreover, additional policy measures announced are expected to provide further support to the mainland and Puerto Rico economy. As a result, the International Monetary Fund now projects an increased rate of 5.1% real GDP growth for the United States in 2021 as compared to the 3.1% projected in October. The CBO, the source of the U.S. mainland forecast for the fiscal plan, has revised the decline in US mainland 2020 real GDP from -5.6% projected in April 2020 to -3.4% presently.
- **The on-island stimulus was larger than anticipated and was executed at faster pace than expected.** The total stimulus from the CARES Act and Puerto Rico government packages is estimated to have exceeded \$14 billion, much of which was spent in FY2020. This represented nearly 20% of on-island GNP and included significant direct support to households (the most immediate form of economic stimulus) such as the expansion of unemployment benefits, the paycheck protection program, and direct payments to Americans. The size and speed of execution of this stimulus helped buffer the economy and led to growth revisions. These upward revisions to stimulus contributed to the softening of the significant blow to the economy of Puerto Rico from the COVID-19 lockdown.
- Nevertheless, growth was partially offset by **the slower reopening of the Puerto Rican economy from the COVID-19 lockdown.** The re-opening of Puerto Rico's economy, expected to occur in early June 2020, did not materialize as envisioned at the time of the last Fiscal Plan submission. Instead, lockdown measures have remained in place well beyond this date. Partial lock-down policies continued, reflecting the persistent and resurgent outbreaks amid a policy shift that utilized lockdowns to prevent outbreaks and viral spread as opposed to ensuring medical treatment capacity. Executive Orders to fight the COVID-19 pandemic utilized lockdowns, curfews, and other measures to reverse economic openings as the original ten-week timeline proved ineffective at stopping the virus. Partial re-openings were quickly reversed, taking a steep toll on growth in the period March through June and key sectors such as tourism were severely impacted, reflecting the persistence and intensity of outbreaks continuing into the fall of 2020.

For FY 2021, the recovery of 0.5% envisioned in the May 27, 2020 Certified Fiscal Plan is now projected to reflect a real economic decline of approximately -3.6% for the fiscal year ending in June of 2021. This downward revision reflects the latest economic activity coincident indicators

through December, which, notwithstanding significant stimulus in the first half of FY2021, show a steep deterioration in real economic activity. Through December 2020, the Puerto Rico Planning Board’s indicators of contemporaneous economic activity has declined by six percent (with respect to the same month in 2019). The projected annual decline reflects gradual attempts to reopen the economy followed by reversals and the loss of businesses amid new surges in COVID-19 cases, as outlined above. At present, the pace, timing and effectiveness of vaccine distribution and subsequent measures to fully reopen the economy remain uncertain. For FY2021, growth estimates assume adjustments to partial and intermittent lockdowns, with some recovery from the first half declines reflected in the Planning Board’s activity index.

EXHIBIT 4: REAL GNP GROWTH RATE AND INFLATION AFTER MEASURES, STRUCTURAL REFORMS, AND DISASTER RELIEF FUNDING



The baseline economic outlook model, which forecasts GNP growth, primarily relies on a comprehensive dataset on the Puerto Rican economy from 1965 to 2017.⁸ It includes dozens of variables that collectively describe the Puerto Rican economy (e.g., growth, population, capital stock, etc.), and is largely impacted by four major factors: (a) the pre-hurricane trendline of Puerto Rico, (b) impacts from the shocks of hurricanes, earthquakes, and COVID-19 on economic activity, employment and the capital stock, (c) the stimulative impact of federal and local relief assistance for hurricanes, earthquakes, and COVID-19, and (d) proposed government efficiency measures and structural reforms.

The 2021 Fiscal Plan includes the most recently published revision to the International Monetary Fund Fiscal Affairs Department’s estimates of capital depreciation. The IMF publishes estimates of capital depreciation of public and private capital stocks, as well as capital stocks from public-private partnerships (PPPs), drawn from analyzing a comprehensive sample of around 170

⁸ The forecast is developed and maintained by DevTech Systems, Inc. using their Macroeconomic Assessment and Public Sector Sustainability MAPSS© forecasting model. It is applied to Puerto Rico using a 60-year comprehensive dataset and applying statistical regressions to show the effects of multiple yet distinct inter-related components of past hurricanes, exogenous developments, and economic policies on growth and inflation. The Government transparently delivers the data, regression estimates, and all other relevant modeling information in spreadsheet form to the Oversight Board along with the fiscal plan. The same spreadsheet-based presentation of the model is also made available to financial advisors in the data room and to other parties upon direction from the relevant authorities.

countries starting from 1960 until 2017. The IMF now estimates a lower rate of depreciation, which in turn increases Puerto Rico's capital stock and consequent expected growth rate going forward. Hence, capital investment undertaken in Puerto Rico have been updated with the new depreciation rate and reflects higher potential GNP growth due to a better capital stock.

The 2021 Fiscal Plan also relies on the Congressional Budget Office (CBO) US inflation projections along with global forecasts of oil and food prices from the IMF's World Economic Outlook. Puerto Rico inflation projections have been updated to reflect the latest inflation trend through 2020, which includes the onset of COVID-19, the ongoing recovery in global oil prices, and the demand shock and caused by government lockdown measures to slow the spread of COVID-19. Given these effects, the 2021 Fiscal Plan forecasts constrained inflation averaging 0.35% across FY2020 and FY2021, similar to FY2019 inflation, and followed by a reversion back to a longer-term trend from FY2022 – FY2023.

4.1 Impact of the global COVID-19 pandemic

In response to the global COVID-19 pandemic, the economy of Puerto Rico virtually ground to a halt as the public health imperative for people to stay home resulted in all but the most essential workers unable to travel to their places of business. While the approval of vaccines has brought some potential resolution, there is still significant uncertainty about the future of the global, US mainland and Puerto Rican economies.

There is no precedent for the economic shock to Puerto Rico from the COVID-19 lockdowns in the historical dataset that informs the macroeconomic model included as part of the 2021 Fiscal Plan. As such, there is considerable uncertainty around the near-term economic outlook, as there remains a wide range of potential public health and economic outcomes for Puerto Rico, the nation, and the world.

Impact of COVID-19 on the U.S. economy

Consistent with past practice, the Government primarily relies on US government economic forecasts as a principal driver of the general economic conditions of the economy of Puerto Rico. On February 1, 2021, the CBO released its forecast of US GDP growth for 2021-31, showing a real GDP decline of -3.4% in calendar year 2020, followed by a recovery of +4.6% in calendar year 2021.⁹ The 2021 Fiscal Plan uses this forecast as a key input to create the forecast for the economy of Puerto Rico. The longer-term U.S. growth projections provided by CBO reflect a material improvement relative to the CBO projections of U.S growth from a year ago.

The economy of Puerto Rico suffers directly from Covid-19 related lockdowns, curfews, and other measures, and indirectly from lost revenue (e.g., tourism) from U.S. mainland lockdowns. Of course, while the Puerto Rican economy is currently experiencing an overwhelmingly negative impact from COVID-19, it is possible that the economy could see some benefit from the crisis over the long-term. For example, if concerns over global supply chains result in increased domestic pharmaceutical and medical supply manufacturing, and Puerto Rico is able to play a leading role in the national portfolio of locations where this manufacturing relocates, the Island could experience positive growth as a result. Additionally, there will likely be more Federal stimulus in the short-run or could be material changes to the transfers Puerto Rico receives from the Federal Government. However, given their uncertain nature, the 2021 Fiscal Plan does not account for these potential scenarios. This includes the third major Coronavirus stimulus bill, the American Rescue Plan Act of 2021, which passed in the U.S. Senate on March 6, 2021. Nevertheless, from an economic modeling perspective, there is significant uncertainty about the final bill (given the

⁹ CBO's Current Projections of Output, Employment, and Interest Rates and a Preliminary Look at Federal Deficits for 2020 and 2021.

differences in the House and Senate versions), as the Act returns to the House of Representatives on March 9, 2021 and then to the White House for the President's signature.¹⁰

The 2021 Fiscal Plan also does not explicitly include its own independent assumptions about the effectiveness of global, US federal, and Puerto Rico measures to contain the spread and impact of COVID-19, and particularly, the advent of vaccines or other countermeasures. Rather, the Government relies on the embedded assumptions included in the CBO and IMF global and US growth scenarios to reflect these.

Specific impacts of COVID-19 on the economy of Puerto Rico

After incorporating US mainland growth estimates, the 2021 Fiscal Plan forecasts the specific impacts of the pandemic on Puerto Rico. The approach accounts for two primary factors, which are outlined below: (i) lost income from an enduring spike in unemployment, and (ii) the relative amount of income that will be replaced either directly by extraordinary government support programs or indirectly as a pass-through from non-labor forms of federal and local spending on the response (e.g., on public health infrastructure, distance learning for education).

To determine the lost income due to COVID-19, the Government has analyzed available public and private sector forecasts of US unemployment and data from initial unemployment claims through early January 2021. As of February 20, 2021, there were 28,927 continued claims for unemployment in Puerto Rico and 1,275 new claims filed. This represents a return to the historical trends of approximately 2,360 initial claims filings per week.¹¹ The below exhibits, illustrate the trends in Puerto Rico's initial claims and continued claims since the beginning of the COVID-19 pandemic.

¹⁰ See H.R.1319 - American Rescue Plan Act of 2021, track legislative progress on the 117th Congress <https://bit.ly/3cnr33J>.

¹¹ United States Department of Labor, Employment & Training Administration, Unemployment Insurance Weekly Claims Data. Historical trend represents the weekly average from January 2, 2010 through March 14, 2020.

EXHIBIT 5: PUERTO RICO UNEMPLOYMENT ACTUALS WEEKLY INITIAL CLAIMS

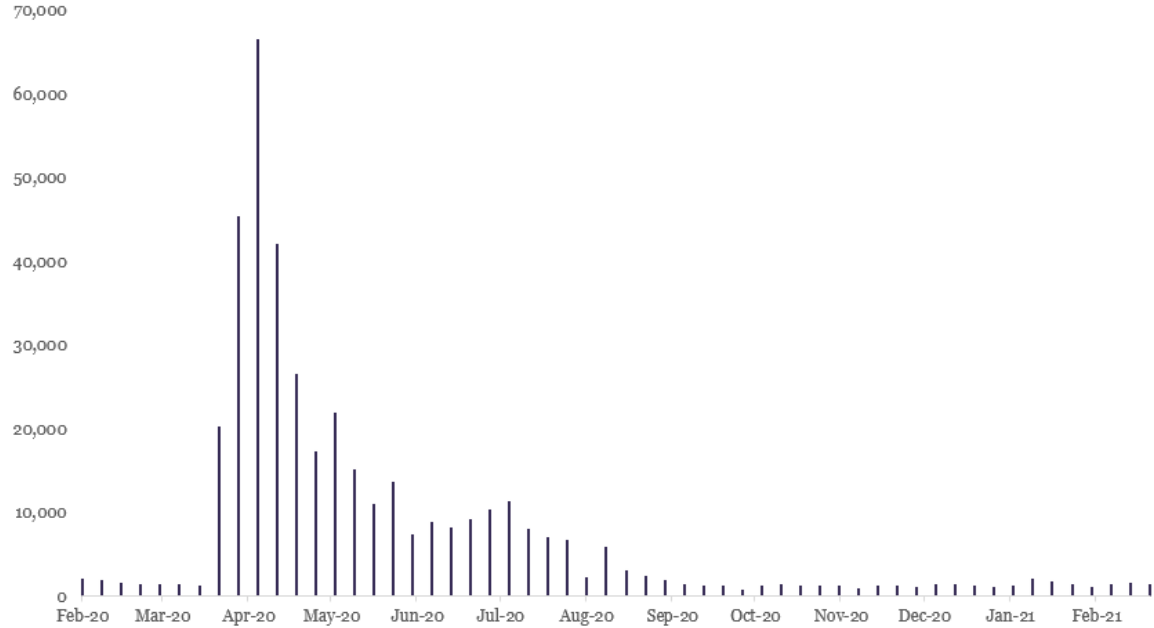
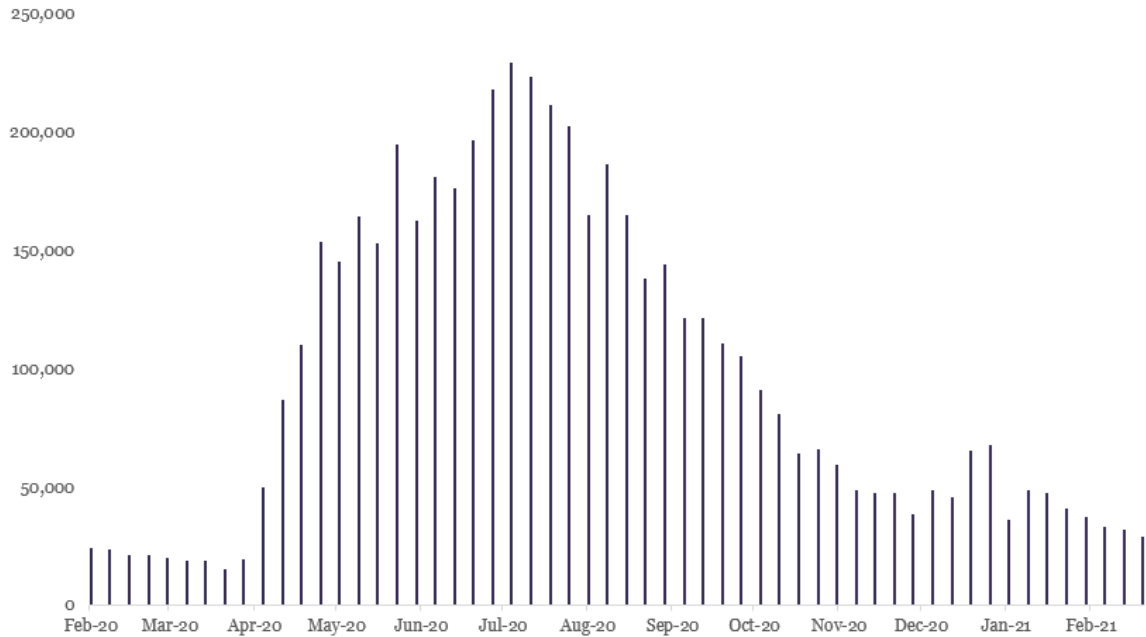


EXHIBIT 6: PUERTO RICO UNEMPLOYMENT ACTUALS CONTINUED CLAIMS



The size of the total economic shock to Puerto Rico is scaled through a regression analysis of the relationship between the economic cycle of Puerto Rico and the observed unemployment, which is then fit to the observed data. The size of the direct impact of Covid-19 containment policies on the island’s economy is measured as the difference between the U.S. Mainland shock to Puerto Rico, and the total Covid-19 economic shock to the island. The total unemployment includes observed unemployment claims, self-employed persons receiving Covid-19 related benefits, and

estimates of employment supported by PPP Program Loans. The latter are derived using U.S. Treasury data of PPP Loan Program beneficiary firms made publicly available in 2020, which report jobs and loan amounts. The unemployment shock at the beginning of the lockdown can be compared with the Great Recession to develop the magnitude of the shock and its impact on firms' job shedding, and then back out an estimate of the program's impact on firms during its period of implementation.

In light of ongoing economic hardship for the people of Puerto Rico, and the United States as a whole, federal and local governments continue to provide much needed economic support for residents on the Island. The following sections describe how the 2021 Fiscal Plan treats the combined impact of ongoing disaster relief funding, as well as more recent economic support in light of COVID-19 related stimulus packages and other changes to fiscal transfers.

4.2 Federal and local relief spending for Hurricanes Irma and Maria, earthquakes, and the global COVID-19 pandemic

4.2.1 Disaster relief spending from the 2017 Hurricanes

Disaster spending tends to have a short-term stimulative effect on an economy post-crisis, though not in the long term. In Puerto Rico, the level of committed public and private disaster relief spending is significant when compared to the overall size of the economy. Public and private disaster relief spending has and will continue to impact the economy in two ways:

- **Stimulative impact from post-hurricane disaster relief spending that is greater than 100% of the Island's 2018 GNP.** This stimulus can come in multiple forms, such as construction companies hiring local, unemployed workers or workers from the mainland United States paying local withholding taxes and spending money for food and lodging.
- **Expected reconstruction of the capital stock on the Island.** The 2021 Fiscal Plan factors in significant damage to the capital stock that is repaired, in large part, by this significant infusion of federal and private monies, contributing to growth in the long-term.

The 2021 Fiscal Plan projects that ~\$86 billion of disaster relief funding in total, from federal and private sources, will be disbursed in the hurricane and related reconstruction effort over a period of 15 years¹². It will be used for a mix of funding for individuals (e.g., reconstruction of houses, personal expenditures related to the hurricane such as clothing and supplies), funding for the public (e.g., reconstruction of major infrastructure, roads, and schools), and to cover part of the Commonwealth's share of the cost of disaster relief funding (recipients often must match some portion of federal public assistance spend).¹³

Of the total, ~\$50 billion is estimated to come from FEMA's Disaster Relief Fund (DRF) for Public Assistance, Hazard Mitigation, Mission Assignments, and Individual Assistance. An estimated \$8 billion has been disbursed related to private and business insurance pay outs. An additional \$8 billion is related to other sources of federal funding.

The 2021 Fiscal Plan includes ~\$20 billion from the federal Housing and Urban Development (HUD) Community Development Block Grant - Disaster Recovery (CDBG-DR) program, of which ~\$2.4 billion is estimated to be allocated to offset the Commonwealth and its associated

¹² Revised DRF projections included in the 2021 Fiscal Plan are based on updated information provided by COR3. While the forecast goes through FY2032, the majority of DRF-related spending is forecast to occur over a 13-year period from FY2018 to FY2030.

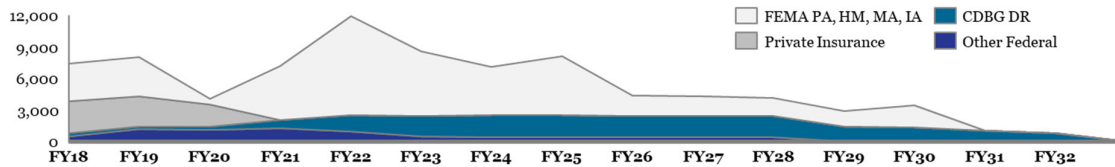
¹³ Puerto Rico's cost-match responsibility was estimated using FEMA-provided data, adjusted by category as necessary for waivers and exceptions.

entities' expected FEMA-related cost-share requirements.¹⁴ This portion of CDBG-DR funding will go towards covering part of the ~10% cost-share burden on expenditures attributable to the Commonwealth, PREPA, PRASA, and HTA. The 2021 Fiscal Plan allocates ~\$2.6 billion for Puerto Rico's out-of-pocket cost-match responsibility, including the provision of \$600 million for Commonwealth cost-match reserve funding in case fewer CDBG-DR funds than anticipated become available in a given year.

EXHIBIT 7: PROJECTED PRIVATE AND PUBLIC DISASTER RELIEF FUNDING ROLL OUT

	FY18 \$M	FY19 \$M	FY20 \$M	FY21 \$M	FY22 \$M	FY23 \$M	FY24 \$M	FY25-32 \$M	Total \$M	Total %
FEMA PA, HM, MA, IA 	\$5,677	\$3,851	\$746	\$5,136	\$9,480	\$6,128	\$4,640	\$14,681	\$50,339	58.4%
	11.3%	7.7%	1.5%	10.2%	18.8%	12.2%	9.7%	29.2%		
CDBG-DR 	\$320	\$190	\$258	\$794	\$1,556	\$1,980	\$2,081	\$13,044	\$20,233	23.5%
	1.6%	0.9%	1.3%	3.9%	7.7%	9.8%	10.3%	64.5%		
Private Insurance 	\$3,001	\$2,895	\$2,104	\$0	\$0	\$0	\$0	\$0	\$8,000	9.3%
	37.5%	36.2%	26.3%	0.0%	0.0%	0.0%	0.0%	0.0%		
Other Federal Funding 	\$509	\$1,237	\$1,147	\$1,272	\$940	\$499	\$430	\$1,530	\$7,564	8.8%
	6.7%	16.3%	15.2%	16.8%	12.4%	6.6%	5.7%	20.2%		
Total	\$9,506	\$8,173	\$4,256	\$7,202	\$11,976	\$8,607	\$7,150	\$29,255	\$86,125	100%
Spending as a % of GNP	14.0%	11.5%	6.1%	10.6%	17.4%	12.1%	9.8%	38.1%		
CDBG cost share	\$0	\$0	\$0	\$211	\$279	\$255	\$316	\$1,289	\$2,350	

Disaster aid by source of funding, \$M



1 Federal Public Assistance, Hazard Mitigation, Mission Assignments, and Individual Assistance

The major sources of disaster relief funding are detailed below:

- **FEMA Disaster Relief Fund:** FEMA provides Individual Assistance to individuals and families who have sustained uncovered losses due to disasters. FEMA also provides Public Assistance to state and local governments and certain types of private not-for-profits for debris removal, emergency protective measures, and permanent repair to damaged or destroyed infrastructure. Through both its Public Assistance Program and Hazard Mitigation Grant Program, FEMA funds projects to reduce or eliminate long-term risks to people or property from future disasters.¹⁵
- **HUD Community Development Block Grant - Disaster Recovery (CDBG-DR):** HUD provides CDBG-DR funding that can be used for assistance to individuals, businesses, state agencies, non-profit organizations, and economic development agencies. Funds are to be used in the most impacted and distressed areas for disaster relief, long-term recovery, restoration of infrastructure, housing assistance, and economic revitalization. The 2021 Fiscal Plan assumes, based on the supplemental appropriation included in the Bipartisan Budget Act of 2018, that ~\$2 billion will be used to repair the Island's electric infrastructure

¹⁴ Estimate based on early assessment of CDBG-DR Action Plans for Puerto Rico (as published on March 31, 2020), as well as patterns of cost share coverage from CDBG-DR in historical storms.

¹⁵ The 2021 Fiscal Plan does not attribute economic impact to FEMA's Administrative funding, which is used for FEMA's personnel (primarily outside of Puerto Rico), travel, and other internal costs.

and ~\$2.4 billion will be used to cover cost-share for the Commonwealth and its instrumentalities.¹⁶

- **Private insurance funding:** Large personal property and casualty losses have been incurred in the aftermath of Hurricane Maria. An analysis of data from the Office of the Insurance Commissioner of Puerto Rico, adjusted for self-insured and other types of coverage was used to determine the amount that has been paid out to individuals and businesses for major damages.
- **Other supplemental federal funding:** Additional federal funding has been appropriated to various agencies and projects in Puerto Rico following the hurricane. This money is directed at a wide range of recovery efforts, from reconstruction of damaged buildings (for example, funding to repair damage to Job Corps centers in Puerto Rico) to funding for health programs and environmental management (e.g., USDA funding to repair water systems in rural areas) to additional funds for the Nutritional Assistance Program (NAP). Additionally, this includes the \$595 million for the 2020 earthquake disaster funding in FY2020-2023, as outlined below.

Disaster roll out for FEMA funds has been projected by subcategory to account for differences in when funds are spent:

- Individual Assistance from FEMA was spent in the immediate aftermath of the storm.
- Public Assistance Categories A & B and Mission Assignments are used for debris removal and emergency work, and therefore exhausted in the early years of the recovery.
- FEMA Categories C-G and Hazard Mitigation are longer-term funding streams that are spread out over the next ~10 years, based on the latest estimates regarding the time that it will take to finalize reconstruction.

The 2021 Fiscal Plan estimates disaster relief spending based on when funds are expected to be *disbursed*¹⁷. The forecast amounts included are based on the latest actual spending data and projections received from COR3. CDBG-DR funds include program types informed by the Puerto Rico Department of Housing's latest available Action Plans.

As stated before, disaster relief funds will impact the economy in a number of ways: building the capital stock of the Island by constructing, repairing, or replacing damage to buildings, utilities, or other physical goods, directly through consumption of goods and services on the Island, or funding programs and services on the Island. The 2021 Fiscal Plan estimates the rate of pass-through to the economy for these different types of funding as follows:¹⁸

- A 100% pass-through rate is assumed for funding that is used directly and in full to replace income or stimulate spending on goods and services originating on the Island. Hence, this corresponds to the final consumption expenditure that are spent on the Island for immediate disaster relief needs, and that are financed by transfer payments from Federal Disaster Relief Spending funds. This kind of current expenditure or final consumption expenditure on relief

¹⁶ As per the Puerto Rico Disaster Recovery Action Plan, April 2020, "the cost share matching requirements of many of these [FEMA] programs create a financial burden on subrecipients that will dramatically hinder the recovery process without supplemental funding. To substantially reduce this burden, PRDOH intends to leverage CDBG-DR to meet these matching fund requirements..."

¹⁷ Prior Certified Fiscal Plan assumed DRF funding at the mid-point of when funds were expected to be disbursed and obligated. The 2021 Fiscal Plan estimates DRF spending when the funds are expected to be disbursed, based on information provided by COR3.

¹⁸ Estimated using local contracts for PREPA, residential construction and school construction. These contracts were estimated to have between 10% and 18% pass-through on the economy, respectively, which was then augmented by 5.5% average spend on transportation and logistics on construction projects, which rely on 100% domestic labor.

goods and services does not contribute to the capital stock on the Island, and therefore does not contribute to long-term growth.

- An 18% pass-through rate is assumed for all other funding, including funding used to construct, repair, and replace buildings, utilities, and other physical goods, or funding directed toward programs and services on the Island. The pass-through of 18% consists of a base pass-through rate of 12.5% based on a combined top-down and bottom-up analysis of historical FEMA contracts and Government Accountability Office (GAO) data on FEMA spending that includes all categories of reconstruction spending, including capital projects (both utility related and other) and spending on programs and services. It is increased by a 5.5% addition for on-cost logistics for a total pass-through rate of 18%. The 18% represents the portion of funding spent on-Island for labor and on-Island services. The remaining 82% corresponds to capital expenditures or fixed capital formation, and consists of spending on goods and services intended to create future benefits such as infrastructure investment in transport, health, communication, education, etc.
- CDBG-DR funds put toward cost share are not passed through to the economy (0% pass through rate). These funds are used towards the local share of FEMA projects whose value is already accounted for in the respective categories.

4.2.2 Federal and local economic support in response to the earthquakes

The 2021 Fiscal Plan includes \$595 million in funding from FEMA to cover the damage caused by the earthquakes. The earthquake related federal funding is assumed to impact the economy from FY2020 through FY2023.

4.2.3 Federal and local economic support in response to the COVID-19 pandemic

In response to the COVID-19 pandemic, both the Federal Government and Puerto Rico Government launched major relief packages to contain and mitigate the spread of the pandemic, support residents and frontline workers, and help the Island's economy rebound.

On March 6, 2020, President Trump signed an \$8.3 billion emergency COVID-19 aid package. At least \$1.05 billion of this package was to be distributed to state, local, and tribal government efforts through grants and cooperative agreements with the Centers for Disease Control and Prevention or as reimbursements from the Federal Government. The initial federal aid package was focused largely on addressing public health concerns.

On March 13, 2020, President Trump declared a national emergency in response to the COVID-19 pandemic. The declaration allowed the administration to utilize the Stafford Act, a federal law governing disaster-relief efforts and makes \$50 billion in emergency funding available to states and territories.

On March 18, 2020, the Families First Coronavirus Aid Package was signed into law. The bill included free COVID-19 testing for uninsured individuals, emergency paid sick leave, expanded family and medical leave programs, unemployment assistance, food aid and federal funding for Medicaid.

On March 23, 2020, the Puerto Rico Government, with the support of the Oversight Board, announced a package of direct assistance to workers and businesses amounting to approximately \$787 million, of which \$500 million was incremental new spending (made available via a special appropriation), \$131 million was for education related materials through existing federally funded government contracts, and \$157 million was reapportioned within the FY2020 Commonwealth General Fund budget. The budget for this Emergency Measures Support

Package was certified by the Oversight Board on April 2, 2020. At the time, the Emergency Measures Support Package was larger than any stimulus announced so far by any U.S. state or territory¹⁹, and the measure was designed to provide targeted and meaningful support during the early days of the COVID-19 pandemic.

On March 27, 2020, A third phase of federal COVID-19 relief, the Coronavirus Aid, Relief, and Economic Security (“CARES”) Act, was signed into law. The relief package allocated an estimated \$2.2 trillion—the largest fiscal stimulus package in modern American history—to mitigate the harmful effects of the COVID-19 pandemic. It aimed to financially support both governments and businesses, provide direct relief to individuals, and expand COVID-19 response measures, as well as build future resiliency. The CARES Act included \$150 billion of direct support to state and local governments. In addition, eligible individuals received a \$1,200 direct payment, as well as an additional \$500 for each dependent child, in each case subject to income phase-outs. The law also provided for additional unemployment insurance benefits for individuals impacted by COVID-19, including incremental benefits of \$600 per week through July 31, 2020 and a 13-week extension in the amount of time than an individual could collect benefits (from 26 to 39 weeks). On April 24, 2020, the US government passed the Paycheck Protection Program and Health Care Enhancement Act, which can be considered as an extension of the CARES Act. This package provided an additional \$482 billion for small businesses, healthcare providers, and expanded testing to address the COVID-19 pandemic.

The 2021 Fiscal Plan includes an estimate, shown in below, of what portion of these federal funds are estimated to be allocated to Puerto Rico; relying on a combination of direct Federal Government sources and agency announcements, and, in some cases, based on historical analogy.

EXHIBIT 8: ESTIMATED CORONAVIRUS AID, RELIEF, AND ECONOMIC SECURITY ACT (“CARES ACT”) FEDERAL FUNDS ALLOCATED TO PUERTO RICO (\$M)

#	Title	Ref	Section	Est. Actuals (Puerto Rico)		
				Spent	Remain.	Total
1.	Unemployment Assistance	[a]	2102 (33), 2104 (38)	6,329	-	6,329
2.	Recovery Rebates for Individuals	[b]	2201 (55)	2,734	-	2,734
3.	Coronavirus Relief Fund	[c]	5001 (221)	1,906	334	2,241
4.	Paycheck Protection Program	[d]	1102, 1106 (6), Amend.	1,838	-	1,838
5.	Education - Title XII (284)	[e]	Title XII (284)	237	504	740
6.	All Other CARES Act Programs	[f]	Multiple	805	-	805
7.	Total, CARES Act and Related			13,848	838	14,686

[a] As of Jan'2021. Source: Hacienda. Note, this includes multiple federal programs, such FPUC (\$600/week program), as well as federal payments of PUA, PEUC, EB, etc. Additionally, amounts include lost wages assistance program.

[b] As of 1/25. Source: Hacienda.

[c] As of 1/22/2021. Source: AAFAP.

[d] As of 8/8/20. Source: https://www.sba.gov/sites/default/files/2020-08/PPP_Report%20-%202020-08-10-508.pdf

[e] Includes Elementary and Secondary School Emergency Relief Fund, Higher Education Emergency Relief Fund, Governor's Emergency Education Relief Fund. Source: <https://covid-relief-data.ed.gov/profile/state/PR>

[f] Reflects various programs with forecast amounts less than \$200 million. Assumes actual spent was equal to forecast amount per 2020 Fiscal Plan.

Above figures are in millions.

While the local and federal funds have played an essential role to mitigate the unprecedented economic damage from the sudden economic shock caused by the pandemic, additional assistance was necessary to continue addressing the ongoing needs. On December 27, 2020, President Trump signed the Coronavirus Response and Relief Supplemental Appropriations

¹⁹ Puerto Rico unveils record \$787M package to fight COVID-19 ([AP News](#)).

(“CRRSA”) Act of 2021 which provided an additional \$900 billion in COVID-19 relief. The CRRSA allocated no additional funds to states and territories, but it extended the deadline to use Coronavirus Relief Funds, Title V of the CARES Act, by one year as well as provided economic support to businesses and funding to promote testing, contact tracing and vaccine distribution. The 2021 Fiscal Plan estimates that Puerto Rico will receive ~\$6.0 billion of additional federal funding from the CRRSA. This is primarily composed of Direct Payments to Citizens for \$600 per person (~\$1.4 billion), the ESSER Fund (~\$1.3 billion), Small Business Provisions (~\$1.1 billion), Expanded Unemployment Benefits (~\$1.0 billion) and other miscellaneous programs (~\$1.2 billion).

As discussed above, on February 26, 2021, the U.S. House of Representatives passed the American Rescue Plan Act of 2021 which sets the course for Puerto Rico to receive a portion of the \$1.9 trillion of additional pandemic response funding. Among the many possible impacts to Puerto Rico, the key components of the pending legislation include Direct Payments to Citizens of \$1,400 per person plus an additional \$1,400 per dependent, Expanded Unemployment Benefits, and \$350 billion of direct support to state, municipal and county governments. The March 6, 2021 passing of the Act by the Senate will return the bill to the U.S. House of Representatives to approve the law. Of note, there are differences in the House and Senate versions of the Bill. The 2021 Fiscal Plan does not incorporate the potential use of funds from the pending legislation as it is not final at the time of submission. When the bill is signed into law, the Puerto Rico Government will move quickly to ensure the highest and best use of any funds made available to Puerto Rico.

Throughout the COVID-19 pandemic, the Puerto Rico Government has continued to address three core impact areas in an efficient, expeditious and compliant manner. These core impact areas included: public health, economic support, and government operations, and at the time that Puerto Rico published its Strategic Disbursement Plan, the document outlining its plan to use the \$2.2 billion allocated under the CARES Act, on May 15, 2020, Puerto Rico was just one of roughly a dozen states to release a comprehensive plan for allocating CRF funds. Furthermore, Puerto Rico has remained in the forefront of transparent and expeditious use of CRF funds. As of the December 31, 2020 report to the Office of the Inspector General²⁰, Puerto Rico ranked in the top 3% in total dollars spent and in the top 22% in percentage of awarded dollars spent, out of 756 entities who received CRF funds.

²⁰ <https://www.pandemicoversight.gov/track-the-money/funding-charts-graphs/coronavirus-relief-fund>.

EXHIBIT 9: CORONAVIRUS RELIEF FUND DISBURSED & OBLIGATED (\$M)

Program	Current Allocation	Disb. & Obl.
Assistance Program to Private Hospitals	315.0	314.2
Transfer to the 78 Municipalities for Eligible Expenses	300.0	200.0
Allocation to the Unemployment Trust	300.0	300.0
Assistance Program to Self-Employed Individuals	200.0	190.1
COVID-19 Testing and Contact Tracing Program	150.0	140.3
Assistance Program to Small Businesses	124.1	122.3
Acquisition of Materials and Personal Protective Equipment	120.0	118.3
Other Programs (1)	103.0	99.1
Assistance Program to the Tourism Industry	100.0	81.7
Remote Learning Solutions for Students	90.0	79.9
Remote Work Program of the Government of Puerto Rico	90.0	88.6
Emergency Assistance – Public Hospitals	75.0	73.4
Business Interruption Grants	65.0	21.6
Private Sector Payroll Protection Program	56.7	56.7
Reserve	51.9	0.0
Administrative Expenses for Administering PR's CRF	50.0	7.2
FEMANon-Federal Matching Funds Assistance Program	50.0	12.9
TOTAL	2,241	1,906

(1) Other Programs includes Assistance Program to Medium Businesses, Program of Assistance and Care - Homeless Population, COVID-19 Emergency Expenses in Prisons, Telemedicine Program in Puerto Rico, Transfer to United Way, Transfer to PRDE to Reopen Schools.

To properly address the public health emergency, Puerto Rico determined that it must ensure the stability of the healthcare system, implement a robust testing/contact tracing program, and acquire the necessary personal protective equipment. As a result of these targeted actions, Puerto Rico has mitigated some of the public health issues associated with the COVID-19 pandemic. As of February 8, 2021, Puerto Rico had the 9th lowest (out of 56 U.S. states and territories) cases per 100,000 people²¹. Additionally, Puerto Rico's actions minimized the loss of life, and Puerto Rico had the 14th lowest (out of 56 U.S. states and territories) deaths per 100,000 people²². Puerto Rico will continue these efforts through the use of additional COVID-19 relief funds allocated by the CRRSA Act. The CRRSA Act allocated an incremental \$184 million for testing and contact tracing and \$29 million for vaccination *support*, and on January 26, 2021, FEMA approved \$153 million to assist the Puerto Rico Department of Health with distribution and administration of COVID-19 vaccines.

Using federal assistance funds, Puerto Rico developed a robust vaccine distribution plan²³ overseen by the Puerto Rico Department of Health in coordination with the Office of Public Health Preparedness and Response. Vaccine distribution will follow a command structure activated at the state level by the Governor of Puerto Rico and the Secretary of Health with Emergency Operations Centers established via state municipality coordination efforts. Like all states, Puerto Rico is taking a phased approach to COVID-19 vaccination with the assumptions that vaccine supply will be limited early on but will increase quickly over time. With the early doses, Puerto Rico targeted the most at-risk population groups. Exhibit 10 outlines this phased approach for the initial, prioritized population groups.

²¹ Data from Jan 21, 2020 – Feb 8, 2021 at 10:00 am CT (https://covid.cdc.gov/covid-data-tracker/#cases_casesper100k).

²² Data from Jan 21, 2020 – Feb 8, 2021 at 10:00 am CT (https://covid.cdc.gov/covid-data-tracker/#cases_deathsper100k).

²³ <http://www.salud.gov.pr/Documents/coronavirus/PR%20COVID-19%20Vaccination%20Plan.pdf>.

EXHIBIT 10: PUERTO RICO'S INITIAL, PRIORITIZED VACCINE DISTRIBUTION GROUPS

	Population Subgroup	Organization Type	Agency/Organization
Phase 1A	Healthcare Workers in HC Settings	<ul style="list-style-type: none"> Public Hospitals Private Hospitals 	<ul style="list-style-type: none"> ASEM Comprehensive Cancer Center PR Hospital Association
	Long Term Care Facilities Residents	<ul style="list-style-type: none"> State Agency 	<ul style="list-style-type: none"> PR Department of Family Services ASSMCA PR Department of Housing
	People 65 Years of Age and Older	<ul style="list-style-type: none"> Public Health 	<ul style="list-style-type: none"> PRDoH and Municipalities Municipalities College of Pharmacy Walgreens Association of Community Pharmacies
Phase 1B	Other Healthcare Essential Workers	<ul style="list-style-type: none"> Pharmacies Laboratories CDTs and FQHCs Non-Traditional Providers Home Health 	
	First Responders	<ul style="list-style-type: none"> Law Enforcement Emergency Management Firefighters EMS 	<ul style="list-style-type: none"> PREMB
	Critical Infrastructure Workforce	<ul style="list-style-type: none"> Utilities Communications Government Employees Transportation Waste Disposal 	<ul style="list-style-type: none"> PR Department of Transportation
Phase 2	People with Underlying Medical Conditions (1)		
	People Who Are Incarcerated/ Detained in Correctional Facilities	<ul style="list-style-type: none"> State Agency Federal Agency 	<ul style="list-style-type: none"> PR Department of Corrections Federal Bureau of Prisons
	People Experiencing Homelessness/ Living in Shelters		
	People Attending College or Universities	<ul style="list-style-type: none"> Public Universities Private Universities Community Colleges 	
	People Living and Working in Other Congregate Settings	<ul style="list-style-type: none"> Community Based Organizations 	
	People with Disabilities		
	People Who Are Under- or Uninsured	<ul style="list-style-type: none"> Health Insurance 	

(1) Includes people with Cancer; Chronic Kidney Disease ; COPD (Chronic Obstructive Pulmonary Disease) ; Heart Conditions, such as Heart Failure, Coronary Artery Disease, or Cardiomyopathies ; Immunocompromised State (Weakened Immune System) from Solid Organ Transplant ; Obesity (Body Mass Index [BMI] of 30 kg/m2 or Higher but < 40 kg/m2); Severe Obesity (BMI ≥ 40 kg/m2); Sickle Cell Disease; Smoking; Type 2 Diabetes Mellitus.

The road to recovery in Puerto Rico will be lengthy as the destruction of businesses resulting from the COVID-19 pandemic countermeasures will be felt for years to come. To drive important decisions and expedite progress on the road to recovery, Puerto Rico has developed a policy roadmap. Puerto Rico's roadmap to recovery consists of four main pillars: (i) renewing economic support to small businesses, (ii) ensuring continuity of government operations, (iii) safeguarding the stability of our healthcare system and (iv) guaranteeing the efficient distribution of the COVID-19 vaccine.

Renewing Economic Support to Small Businesses: As a result of the actions put in place to slow the spread of the virus, many businesses suffered economic hardships. While some restrictions have been lifted allowing businesses to reopen, small businesses continue to struggle to stay afloat. Small businesses are an integral part of Puerto Rico's economy. The Government of Rico will continue its support to small businesses to ensure they are operational once the COVID-19 pandemic passes.

- Ensuring Continuity of Government Operations:** The Government's mission is to promote economic and public policy initiatives to achieve a better quality of life for all citizens. This can only happen if the government continues to operate, and the Government must ensure it can continue to operate to support the Commonwealth's mission.
- Safeguarding the Stability of the Healthcare System:** Access to high quality healthcare is an important factor in promoting a healthy population. The COVID-19 pandemic has created strain on Puerto Rico's healthcare system which has threatened the existence of many healthcare institutions. The Government will continue to safeguard the stability of the healthcare system to ensure the hospitals can care for the Commonwealth's citizens.
- Guaranteeing the Efficient Distribution of the COVID-19 Vaccine:** Life during the COVID-19 pandemic has been anything but normal, and normalcy cannot be reestablished while citizens continue to die from this deadly disease. A major component to reestablishing

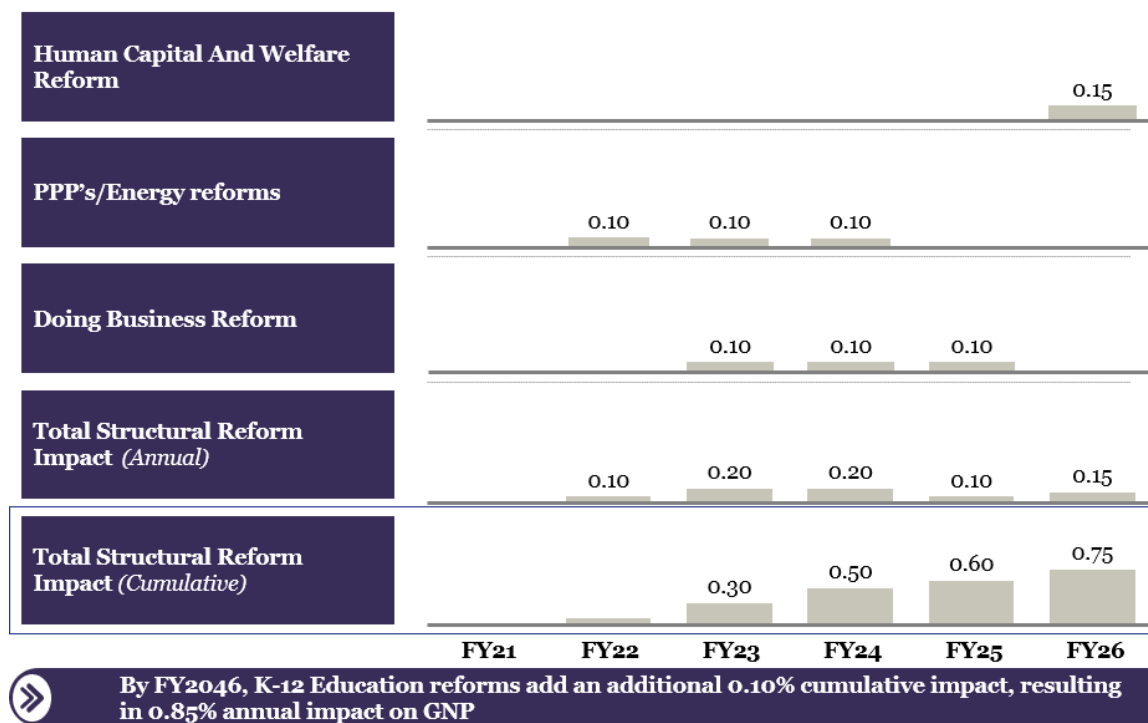
normalcy is through vaccination efforts, and to instill confidence in that effort, the Government will continue the efficient distribution of the COVID-19 vaccine to protect the Commonwealth's citizens.

4.3 Impact of structural reforms

The estimated impact of **structural reforms** is based on work done by the International Monetary Fund on labor reforms implemented in Europe (e.g., Spain and Estonia) and South America (e.g., Peru and Colombia), among other jurisdictions; utilities reform in Latin America; broadly-accepted metrics for measuring improvement in the World Bank's Ease of Doing Business Rankings (as well as case examples of growth experienced by countries that have implemented such reforms); and education reforms in Europe and elsewhere. Structural reform benchmarks, to the extent possible, come from nations or jurisdictions that face similar constraints to Puerto Rico (e.g., limited monetary policy options, high informal labor markets).

Energy and ease of doing business reforms are projected to increase GNP by 0.60% by FY2025, and Human Capital and welfare reform is expected to add another 0.15% in FY2026. Finally, K-12 education reforms add an additional 0.01% annual impact beginning in FY2037, resulting in total GNP increase from structural reforms of 0.75% by FY2026 and 0.85% by FY2046.

EXHIBIT 11: MACROECONOMIC IMPACT OF STRUCTURAL REFORMS



4.4 Population projections

Even before Hurricanes Irma and Maria hit the Island in 2017, Puerto Rico's population had been trending downward by 1-2% every year as residents have left to seek opportunities

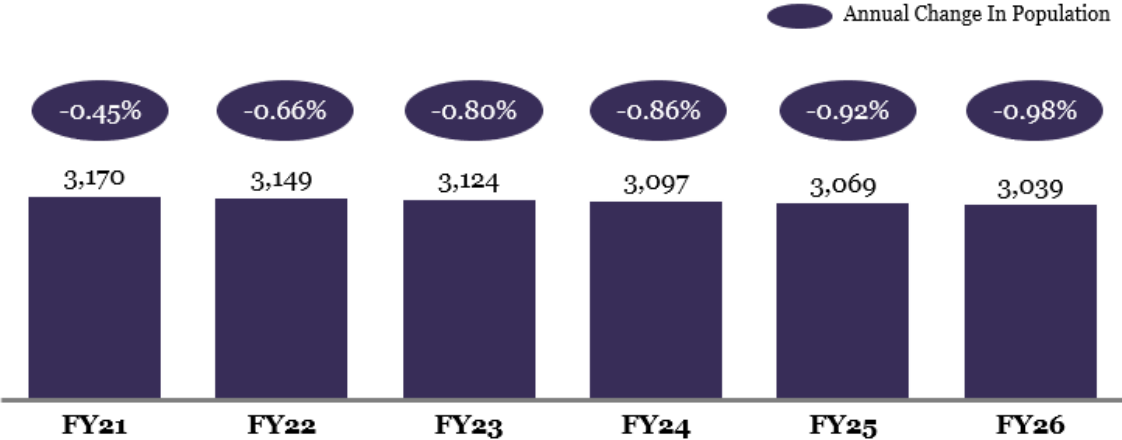
elsewhere and birth rates declined. In 2016, the US Census Bureau's official forecast projected a worsening population outlook due in large part to Puerto Rico's rapidly aging population. This high average age range results from extremely low age-adjusted birth rates and outmigration of younger people. Indeed, in 2016, Puerto Rico began to experience negative natural population change (a higher number of deaths than births). This negative natural change has continued unabated into 2021.

Hurricanes Irma and Maria served to compound the problem, spurring an additional outflow of people just as natural population decline has set in, as many residents lost houses, jobs, and loved ones. While some of these people have returned, the population is still projected to decline over the course of the 2021 Fiscal Plan forecast period and beyond (EXHIBIT 12). Further disasters, such as the series of earthquakes experienced in 2020, have made a swift return to balanced migration less likely. But while net migration is a larger driver of population change in the short term, this factor is volatile; in the long run, net migration is projected to return to more balanced trends. Meanwhile, natural population change is not guaranteed to rebalance at any point, and births are likely to continue declining, while deaths are projected to rise or stay stable.

The COVID-19 pandemic has been less severe in Puerto Rico than in many other areas thus far, and therefore no large epidemic-driven mortality rate increase is anticipated. COVID-19 is expected to suppress air traffic between Puerto Rico and the mainland, and thus impact migration, but this effect will be transitory.

As outlined in the exhibit below, the 2021 Fiscal Plan projects that by FY2025, there will be 3.6% fewer people living on the Island than in FY2020, and that by FY2046, the drop will grow to 24.6%.

EXHIBIT 12: PROJECTED POPULATION CHANGE (POPULATION IN THOUSANDS)



4.5 Impact of First Circuit ruling on Supplemental Security Income benefits

On April 10, 2020, the US Court of Appeals for the First Circuit issued a ruling in a case related to the eligibility of Puerto Rico residents for Supplemental Security Income (“SSI”) benefits (*US v. Vaello-Madero*, 2020). SSI provides “monthly benefits to people with limited income and resources who are disabled, blind, or age 65 or older. Blind or disabled children may also get SSI.”²⁴ SSI benefits have been available to otherwise qualifying residents of the 50 states, the District of Columbia, and the Northern Mariana Islands. Residents of Puerto Rico, however, have not been eligible for SSI benefits.

The case involved an SSI recipient who moved from New York to Puerto Rico and was subsequently required to repay SSI benefits received while the recipient was resident in Puerto Rico. The court ruled in favor of the recipient, finding the exclusion of Puerto Rico residents from SSI coverage to be invalid.

The court’s finding is consequential, but the path forward is highly uncertain. The Trump administration later appealed the decision; however, President Biden has not yet indicated whether the United States will drop its appeal of the case. On March 1, 2021, the U.S. Supreme Court announced that it will hear Puerto Rico’s case on Supplemental Security Income.

If SSI benefits were ultimately extended to eligible residents of Puerto Rico, initial analysis suggests that it could provide over \$1 billion in incremental annual federal transfers to Puerto Rico. This amount would undoubtedly be welcome support to qualifying residents across the Island and could enable some level of increased consumption. The ultimate economic impact of these transfers is unclear, however, and will be examined in future Fiscal Plans. As of the time of certification of the 2021 Fiscal Plan, there is no information as to when and how the benefits will become available to residents of Puerto Rico, how the Government will work with the Social Security Administration to implement the changes, and what program integrity steps will be taken to ensure only those eligible receive it.

Chapter 5. Fiscal Plan financial projections (FY2021-FY2026)

The COVID-19 pandemic has a profound impact on economic growth and, ultimately, on Government revenues. The impact to Puerto Rico is a real GNP decline of -1.4% and -3.6%, in FY2020 and FY2021, respectively. This will change the trajectory of economic activity in Puerto Rico over the entire forecast period.

While COVID-19 continues to have a severe, negative impact on Puerto Rico, the 2021 Fiscal Plan is intended to represent Governor Pierluisi’s vision for a better future for Puerto Rico following the emergence from Title III. As such, the 2021 Fiscal Plan assumes that Puerto Rico will, consistent with President Biden’s commitment for providing Puerto Rico parity in Federal Funding Programs, receive state-like treatment for purposes of obtaining Medicaid federal funding, which represents an ~83% federal matching level for its largest Medicaid population. The additional general fund budget that is available on account of the incremental federal Medicaid dollars is assumed to be used to (i) provide all the needed benefits to improve the coverage and affordability of the health system (such as the long term care and Medicaid premium and cost-share) (ii) to fund the Governor’s initiatives (such as Uniform Remuneration,

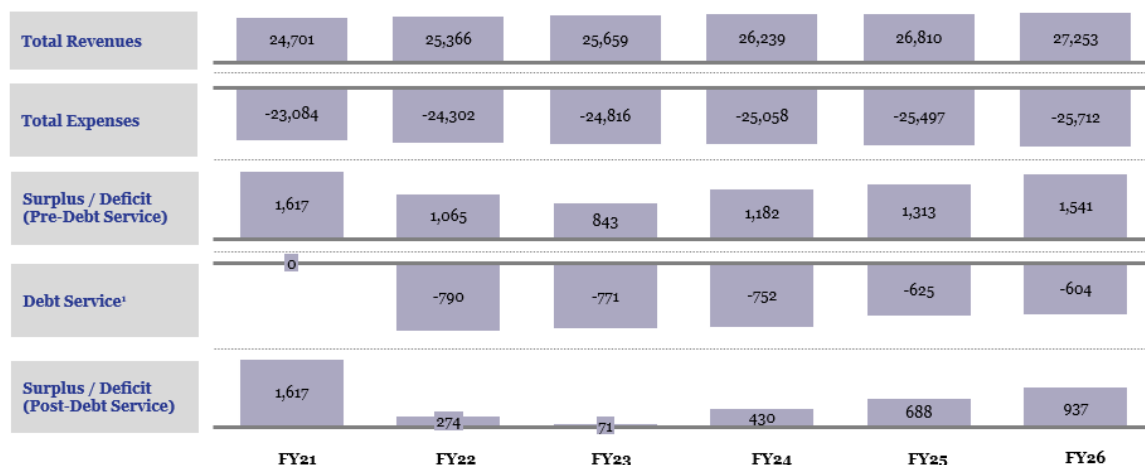
²⁴ Understanding Supplemental Security Income (SSI) Overview -- 2020 Edition, US Social Security Administration.

No more cuts to the UPR and Municipalities, etc.), (iii) and to adjust corporate and personal income taxes to a level that is more in line with other U.S. jurisdictions, thereby improving the business environment and competitiveness of Puerto Rico. As a result of this assumption, the post-debt service²⁵ surplus over the 26-year forecast period from FY21 to FY46 is relatively balanced. This represents a surplus in the early periods, followed by pre-debt service deficits beginning in FY2038²⁶ as over time federal disaster relief funding slows down, Act 154 and Non-Resident Withholding revenues decline, and healthcare expenditures rise at a rate that is faster than Puerto Rico GNP.

Fiscal measures – such as agency efficiency measures, tax compliance & fee measures, and others – are also a significant driver of surplus in the 2021 Fiscal Plan. Fiscal measures have driven and will continue to drive significant surplus. Most fiscal measures have been achieved and are included in the baseline revenue and expenditures. Go-forward cuts to the UPR and Municipalities and pension cuts have been excluded from the 2021 Fiscal Plan, consistent with the new government platform initiatives.

Structural reforms contained in the 2021 Fiscal Plan are also a significant driver of surplus, as these are forecast to account for a cumulative 0.85% increase in growth by FY2046 (equal to ~\$19 billion). However, even after fiscal measures and structural reforms, and before debt service²⁷, there is an annual deficit reflected in the projections starting in FY2038. Exhibit 13 illustrates the projected deficit / surplus through FY2026. Projections for FY2026 onwards are included in *Chapter 1*.

EXHIBIT 13: PROJECTED DEFICIT / SURPLUS (\$M)



(1) Debt Service is tied to the 2021 February PSA.

5.1 Revenue forecast

Major revenue streams include non-export sector General Fund revenues (including individual, corporate, and sales and use taxes) and export sector revenues (including Act 154 excise taxes

²⁵ Reflects the debt service per the February 2021 PSA, which reflects the current agreement between holders of General Obligation and Public Buildings Authority bonds and the Oversight Board. The February 2021 PSA is subject to incorporation in the Plan of adjustment and other definitive documentation and is shown herein for illustrative purposes.

²⁶ Post-debt service deficits begin in FY2033.

²⁷ The February 2021 PSA reflects the current agreement between holders of General Obligation and Public Buildings Authority bonds and the Oversight Board. The February 2021 PSA is subject to incorporation in the Plan of adjustment and other definitive documentation and is shown herein for illustrative purposes.

paid by multinationals operating on the Island, and Non-Resident Withholdings), as well as federal funding. The 2021 Fiscal Plan also includes claw back revenues in the Commonwealth's revenue streams and surplus calculations; this is based on the Government's and Oversight Board's legal conclusions that (i) such monies are property of the Commonwealth, (ii) each statute appropriating or transferring such monies to instrumentalities of the Commonwealth is preempted by PROMESA, (iii) such statutes were enacted by prior legislatures that cannot bind the current legislature, and (iv) in any event, under the Puerto Rico Constitution, such monies would not be transferred to the instrumentalities while General Obligation debt is not being paid according to its terms.

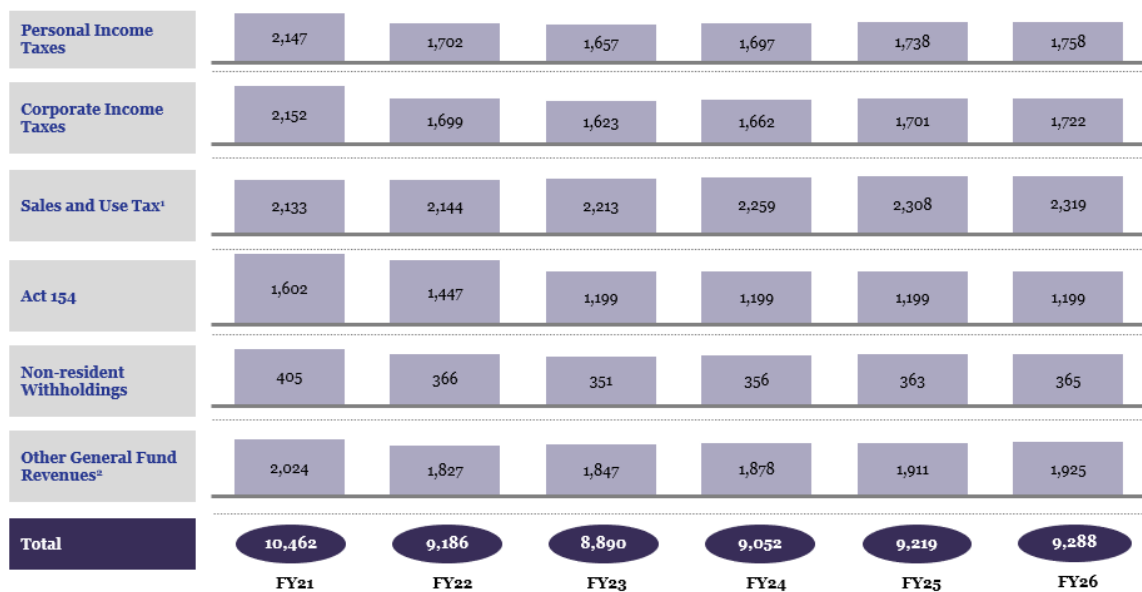
There is expected to be continued near-term uncertainty in the level of revenue collections as the expected duration and severity of the COVID-19 induced recession is constantly evolving. Personal income taxes will be impacted by higher-than-normal unemployment levels, while Consumption taxes will be impacted by lower overall economic activity. The 2021 Fiscal Plan estimates these impacts based on the information currently available and discussions with Hacienda.

Administrative actions taken to delay tax payment due dates in response to the COVID-19 pandemic had the effect of delaying the receipt of ~\$534 million in taxes otherwise due in FY2020 to FY2021 ("COVID-related Tax Deferrals"), according to Hacienda estimates. This includes ~\$224 million related to individual income taxes, ~\$236 million related to corporate income taxes, ~\$36 million related to sales and use taxes, and ~\$39 million related to other general fund revenues. The 2021 Fiscal Plan treats these COVID-related Tax Deferrals as revenue in FY2021.

The long-term vision of Puerto Rico, as outlined in this document, assumes that the Puerto Rico Medicaid program will be properly federally funded, as it is with other mainland jurisdictions. This assumed incremental funding provides for an increase to the general fund budget, which allows for Puerto Rico to provide all the necessary benefits to improve the coverage and affordability of the health system and to improve the tax disparity facing the island's individuals and corporations relative to stateside peers. As such, the 2021 Fiscal Plan assumes that corporate and personal income taxes will be reduced to become more in line with other U.S jurisdictions.

Moreover, shown below represents the major general fund revenue streams after the reduction of the corporate and personal income tax rate reductions.

EXHIBIT 14: MAJOR GENERAL FUND REVENUE STREAMS POST-TAX RATE REDUCTION MEASURES (\$M)



(1) Sales and use tax (SUT) reflects collections after payout of the COFINA settlement.

(2) "Other" general fund revenues include cigarette, rum, motor vehicles, alcoholic beverages, and other general fund taxes.

Note: Above figures include impact of tax rate reduction measures.

Additional details on the fiscal plan revenue streams are provided below, with details on the financial projections included in the Appendix. The following sections describe the longer-term approach to estimating revenues for key revenue streams.

5.1.1 Non-export sector General Fund revenue projections

General fund revenues in FY2021 are projected based on their 6-month actual performance year-to-date plus a re-forecast of the second half of FY2021. The second half re-forecast in FY2021 is calculated based on historical trends and discussions with Hacienda. More specifically, the analysis calculates the historical first half revenues as a percentage the total year revenues from FY2015-2019²⁸, and applies that percentage to actual performance year-to-date in FY2021²⁹.

Individual income taxes: Individual income taxes are highly concentrated, with 78.2% of revenues coming from the 8.7% of returns reporting income above \$60,000 in FY2018.³⁰ Individual income tax collections moderately outperformed the 2020 Liquidity Plan for the first half of FY2021 and have been adjusted to reflect a higher recurring revenue base for individual income taxes moving forward. The 2021 Fiscal Plan projects that disaster recovery spending will continue to contribute to the income tax base, either through mainland workers temporarily working in Puerto Rico or from Puerto Rican residents entering the formal economy as a result of disaster recovery projects. Beginning on October 1, 2022, consistent with the timing of assumed increase in the federal matching percentage to a level similar to that of other U.S. jurisdictions, the 2021 Fiscal Plan assumes that individual income taxes are reduced in an effort to become more in line with other U.S. jurisdictions.

²⁸ Generally, excludes FY2018 given the noise included in the data from the hurricane.

²⁹ Includes adjustments for non-recurring items, such as COVID-related Deferrals and certain Partnership revenues.

³⁰ Hacienda historical reports as of April 2018.

Corporate income taxes: There is also concentration in tax receipts among the largest corporations operating in Puerto Rico (e.g., ~29% of corporate income taxes are paid by 20 corporate taxpayers).³¹ Historical aggregated data from Hacienda showed an influx of corporate activity spurred by reconstruction funding and mainland-based firms entering the Island economy. This had led to higher corporate income taxes relative to GNP in FY2018 and FY2019. Corporate income tax collections moderately outperformed the 2020 Liquidity Plan for the first half of FY2021 and have been adjusted to reflect a higher recurring revenue base for corporate income taxes moving forward. The 2021 Fiscal Plan incorporates the contribution of disaster recovery spending into future years. Moreover, the 2021 Fiscal Plan projections reflect certain adjustments to corporate income tax revenues attributable to the forecast decline in Act 154 companies, which also contribute to normal course corporate income tax collections. Beginning on October 1, 2022, consistent with the timing of assumed increase in the federal matching percentage to a level similar to that of stateside peers, the 2021 Fiscal Plan assumes that corporate income taxes are reduced in an effort to become more in line with other U.S. jurisdictions.

Sales and use taxes (SUT): As with corporate and personal income taxes, SUT outperformed relative to GNP in FY2018 and FY2019, likely boosted by the increased economic activity resulting from the post-disaster reconstruction process (including through the replacement of lost inventory), as well as higher SUT compliance by those larger firms less impacted by the storm. The 2021 Fiscal Plan incorporates this incremental tax collection as disaster recovery continues in future years. As provided in the COFINA Title III Plan of Adjustment, a portion of SUT collections will be used to pay the settlement with COFINA bondholders. This portion reaches approximately \$0.9 billion annually starting in FY2039.

Other General Fund revenue (Motor Vehicles, Alcoholic Beverages, Cigarettes, Other General Fund Revenues): Motor vehicle revenue tax receipts surged in FY2018 and this trend continued into FY2020 and FY2021, as residents accelerated motor vehicles purchases in the aftermath of the storm. In particular, the first half of FY2021 has seen higher than expected vehicle sales with respect to the truck category. The 2021 Fiscal Plan reflects accelerated purchasing of motor vehicles that subsides and returns to historical trends over multiple years. Additionally, Other General Fund Revenues significantly outperformed the 2020 Liquidity Plan for the first half of FY2021 and have been adjusted to reflect higher recurring revenue base for other general fund revenues moving forward. This outperformance is primarily on account of higher-than-expected taxes from partnerships, some of which is expected to be continuous and some of which is expected to be one-time in nature.

Export sector revenue projections: Act 154 and Non-Resident Withholding (NRW) tax revenues are concentrated in a small number of multinational corporations. From FY2017 to FY2023, the 2021 Fiscal Plan estimates that Act 154 and NRW revenues will erode due to US federal tax reform, global supply chain diversification, and patent expirations. The Act 154 tax was enacted in 2010 by the Puerto Rico legislature. It is an excise tax that is creditable in the United States under IRS Notice 2011-29, which remains in effect to date.

On September 29, 2020, the IRS published the Notice of proposed rulemaking REG-101657-20, which proposes new regulations in relation to new definitions with respect to foreign income taxes and taxes paid “in lieu of an income tax”. As currently drafted, the proposed foreign tax credit regulations would have the effect of making Act 154 taxes no longer creditable and would create a serious disruption of the Act 154 tax program, one of the most important sources of revenue the Government has, representing over 15% of general fund revenues in FY2021. The economic impact on the Island would be devastating, putting at risk over 80,000 well-paying American jobs. Changes to this taxation regime will likely force Puerto Rico to change its current

³¹ Hacienda historical reports as of April 2018.

tax system. Any option that we may propose as a substitute will require proper vetting and approval from the U.S. Treasury.

The Government has already begun technical discussions with the U.S. Treasury and submitted on February 9, 2021 comments to the proposed regulations.

The Government has held numerous meetings with U.S. Treasury and leading Act 154 companies and will continue to work collaboratively to find a more permanent and equitable solution that does not threaten Puerto Rico's current tax base, and even more important, the thousands of direct and indirect jobs generated by companies impacted by this change, which is critical to our economic recovery. The ultimate objective is to replace Act 154 with an alternative tax rate structure that maintains Puerto Rico in a competitive position and that will enhance economic development on the Island.

While it is the position of the Government that the proposed rules should not apply to the taxes imposed under Act No. 154 of 2010, as amended, both for policy and for technical reasons, there is no guarantee that the proposed regulations will be changed.

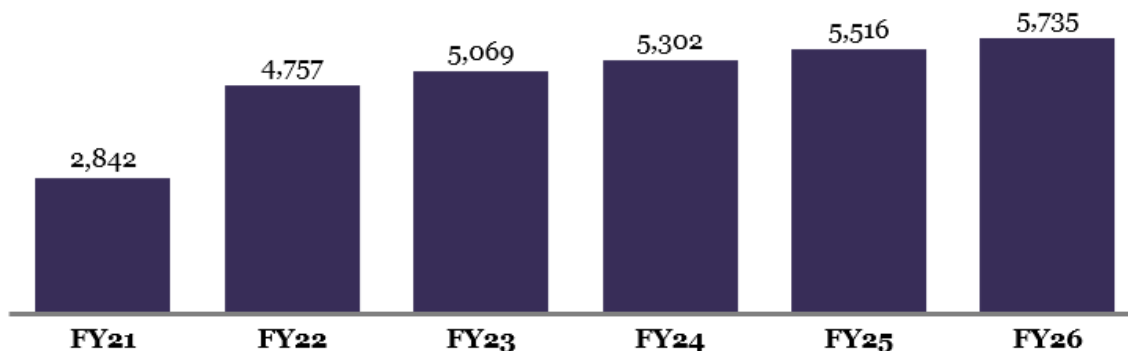
The impact of the proposed regulations, if Treasury concludes that they do apply technically to Puerto Rico, would be to deprive an American territory of significant general fund expenses, potentially cause US companies to leave Puerto Rico which will cause a sharp increase in unemployment, and other forms of economic harm in a territory of the United States that has suffered from a long-term economic recession and a massive hurricane that delayed its economic recovery. Due to the high level of uncertainty related to this matter, current projections have a cumulative reduction of approximately ~43% over the next 11 years.

5.1.2 Medicaid funding

- **Children's Health Insurance Program (CHIP) funding.** CHIP funding is not subject to a federal funding cap. Without additional legislation, the CHIP matching rate (E-FMAP) for Puerto Rico is expected to be 68.5%. Under the Affordable Care Act, the E-FMAP for Puerto Rico was raised to 91.5% through September 30, 2019; under the 2020 Further Consolidated Appropriations Act, the E-FMAP was increased to 83.2% through September 30, 2021 (with an additional 11.5% increase through September 30, 2020 under the 2018 HEALTHY KIDS Act); and under the Families First Coronavirus Response Act, the E-FMAP was increased to 99.0%. Beginning in October 2021, the 2021 Fiscal Plan assumes that Puerto Rico would, consistent with President Biden's commitment for providing Puerto Rico parity in Federal Funding Programs, receive state-like treatment for this program, which would mean unlimited federal financing for the program at an ~88% E-FMAP. The 88% E-FMAP is assumed for the remainder of the forecast period.
- **Increases in available Medicaid funding from federal legislation:** Since 2011, Puerto Rico has received temporary relief from rising healthcare costs through increased levels of federal reimbursement made available through the passage of the Affordable Care Act and the Bipartisan Budget Act of 2018. In December 2019, the Further Consolidated Appropriations Act was passed, which provided supplemental federal funding (up to \$5.7B in total) to Puerto Rico's Medicaid program through September 30, 2021 (i.e., the first quarter of FY2022). In addition, the law raised the FMAP—the portion of Medicaid expenditures that federal funds can cover—from the standard level of 55% to 76% for most populations. Finally, as mentioned above, in response to the COVID-19 pandemic, the Families First Coronavirus Response Act was passed in March 2020, further increasing both the available federal funds (adding an additional \$183M) and the FMAP (increased by an additional 6.2% for most populations). The available supplemental federal funds and higher FMAP will both return to standard levels in October 2021 without new federal legislation. However, the 2021 Fiscal Plan assumes that as of federal fiscal year 2022 (October 1, 2021)

Puerto Rico will, consistent with President Biden’s commitment for providing Puerto Rico parity in Federal Funding Programs, receive state-like treatment in terms of Medicaid funding and program requirements. This would mean unlimited federal financing for the program at an ~83% FMAP for Puerto Rico’s largest population.³² The 2021 Fiscal Plan assumes that Puerto Rico will provide all necessary benefits, such as long-term care and Medicare premium and cost share, which are currently not covered. Such benefits, which can only be afforded with the heightened matching by the Federal Government, will dramatically improve the healthcare system for the residents of Puerto Rico. Exhibit 15 below outlines expected Medicaid federal fund receipts.

EXHIBIT 15: FEDERAL FUNDS RECEIPT PROJECTIONS FOR MEDICAID (\$M)



5.1.3 Other federal funding

In addition to Medicaid funding, Puerto Rico receives other federal funds on a regular basis. These are not to be confused with disaster relief funds, which are directly tied to Hurricane Maria and earthquake reconstruction activity, or with COVID-19 response and relief funds, which are meant to cover incremental government spend to respond to the global pandemic. Examples of these funds include social programs, such as supplemental nutritional assistance (SNAP) and community schools. These funds typically cover both social benefits and operational expenditures. Across these categories, federal fund inflows and outflows are forecast to mirror each other (as benefit needs decline, so do funds), and are therefore surplus neutral to the Commonwealth.

5.1.4 Special Revenue Funds

Commonwealth agency Special Revenue Fund (SRF) revenues: The Commonwealth collects a significant portion of its revenues through Special Revenue Funds, which are funded from, among other sources, tax revenues transferred by statutes, fees and charges for services by agencies, dividends from public corporations and financing proceeds. The baseline level of SRF revenues of Commonwealth agencies (excluding IFCUs) has been updated in this 2021 Fiscal Plan, consistent with the FY2021 budget and FY2022 government budget submission.

Independently Forecasted Component Unit (IFCU) revenues: The Commonwealth contains twelve Independently Forecasted Component Units, which range from public

³² The FMAP assumed for certain populations from October 2021 through December 2021 remains elevated above these amounts on account of the ~6.2% increase from the Families First Coronavirus Response Act.

corporations (e.g., the State Insurance Fund Corporation) to public hospitals (e.g., the Cardio Center). These entities are mostly funded by Special Revenue Funds and may also receive General Fund appropriations. While most IFCU revenues are projected using GNP, given the unique nature of each IFCU, certain revenue streams are grown by other factors, such as inflation, population, or as governed by legislation. The 2021 Fiscal Plan factors in the expected negative impact of the COVID-19 pandemic on demand for government and tourism related services.

Municipal contributions to PayGo: The 2021 Fiscal Plan includes receipts from municipalities to cover retirement expenses incurred by the Commonwealth on their behalf. Since the passage of Act 106-2017, municipalities that participate in ERS are financially responsible for PayGo expenditures covered by the Commonwealth.

Public Corporation PayGo receipts: The 2021 Fiscal Plan includes receipts from public corporations that participate in ERS to cover PayGo expenditures covered by the Commonwealth. The Commonwealth shall be reimbursed for these payments and will act if these contributions are not received (e.g., will withhold payments for utilities).

FAM: The Municipal Administration Fund (FAM) collects 0.5% of the SUT which is distributed into three funds: (1) 0.2% to the Municipal Development Fund; (2) 0.2% to the Municipal Redemption Fund; and (3) 0.1% to the Municipal Improvement Fund (referred to as the FMM). Pursuant to Section 4050.09 of Act 1-2011, the FMM are to be distributed through annual legislation and appropriated for select capital works and improvement.

5.2 Expenditure forecast

In an effort to provide a clear reconciliation between the budget process and the fiscal plan, the expenses included in the 2021 Fiscal Plan are broken out by fund type and by major expense category, as described below. As such, fiscal measures through FY2022 have been trued-up to clearly show the relationship between the fiscal plan and budget processes.

The following exhibit outlines the expenses included in the 2021 Fiscal Plan, by fund type. In doing so, the intention is for full transparency to reconcile the total expenses included in the fiscal plan to the total expenses included in the 2021 and 2022 budgets. For example, the below amount shown of \$10,045 million for the total general fund expenses in FY2021 matches the FY2021 general fund budget. Additionally, the below breakout of expenses for FY2022, by fund type, matches the submission of the FY2022 budget provided by Governor Pierluisi's administration to the Oversight Board, but for certain reconciling items.³³

³³ The reconciling item from the FY2022 government budget submission to the amounts included in the 2021 Fiscal Plan represents the adjustment made on account of (i) changes in assumptions regarding the Medicaid federal matching level discussed throughout the 2021 Fiscal Plan and (ii) assumption that certain initiatives included in the FY2022 budget submission could be funded via the unallocated general fund capital expenditure budget.

EXHIBIT 16: EXPENDITURES, BY FUND TYPE (\$M)

General Fund Expenses	10,045	9,333	9,362	9,209	9,269	9,113
Special Revenue Fund Expenses	3,284	3,251	3,310	3,372	3,434	3,479
Federal Fund Expenses	8,897	10,812	11,213	11,532	11,836	12,147
Other Expenditures Outside of Budget	858	906	931	945	958	972
Total	23,084	24,302	24,816	25,058	25,497	25,712
	FY21	FY22	FY23	FY24	FY25	FY26

Moreover, the following exhibit outlines the same underlying expenses included in the 2021 Fiscal Plan across the major expense categories.

EXHIBIT 17: EXPENDITURES, BY MAJOR EXPENSE CATEGORY (\$M)

GF- Payroll (non-federally funded)	2,891	2,761	2,721	2,754	2,789	2,824
GF- Direct operating expenditures (non-federally funded)	3,478	2,689	2,754	2,605	2,611	2,437
CW Appropriations	973	983	943	878	877	838
Commonwealth Medicaid expenditures	316	470	566	590	611	635
Pension expenditures	2,055	2,114	2,055	2,055	2,049	2,043
Capex	332	316	322	327	332	337
IFCU & CW SRF expenditures	3,284	3,251	3,310	3,372	3,434	3,479
Federally funded expenditures	8,897	10,812	11,213	11,532	11,836	12,147
Other Expenditures Outside of Budget	858	906	931	945	958	972
Total	23,084	24,302	24,816	25,058	25,497	25,712
	FY21	FY22	FY23	FY24	FY25	FY26

5.2.1 General fund payroll and non-personnel operating expenditures

General Fund Payroll expenditures: In the 2021 Fiscal Plan, General Fund payroll for FY2021 and FY2022 are based on the FY2021 budget and FY2022 government budget submission, respectively, for both the Commonwealth agencies and component units. The Commonwealth agencies, which make up the largest portion of spend related to payroll, are forecast to grow at the Puerto Rico inflation rate. IFCU's are forecast in a similar way to the Commonwealth, however not all IFCU have General Fund payroll; ASEM, ASES, ADEA, AAFAP and PRCCDA are forecasted to grow at Payroll and Direct Operating Expenses Inflation, while PRTIA is forecasted to grow at Puerto Rico inflation. Any incremental reductions to baseline

payroll expenditure projections from attrition, absenteeism, or workforce reductions will be captured through fiscal measures.

General Fund Non-personnel operating expenditures: Non-personnel operating expenditures in FY2021 and FY2022 also tie to the budget. Thereafter, non-personnel operating expenditures are assumed to grow by Puerto Rico inflation for the Commonwealth's agencies in addition to the vast majority of the IFCUs. There are select adjustments made as necessary (e.g., for reapportionments).

5.2.2 Special Revenue Funds

Commonwealth Agency Special Revenue Fund (SRF) operational expenditures: The Commonwealth funds a significant portion of its expenses with Special Revenue Funds. Given that SRF revenues and expenditures are not part of the General Fund for budgeting purposes, they are not included in the General Fund budget resolutions approved by the Legislature. However, the Oversight Board has certified SRF expenditures starting with the FY2019 budget process, which are now reflected in the FY2021 and FY2022 budget submissions. With data made available by the Commonwealth, the baseline level of SRF expenses of Commonwealth agencies (including IFCUs) has been updated. SRF expenses are forecast to be equal to the estimated SRF revenues in each year, apart from select incremental SRF-related agency efficiency measures that drive surplus at the Commonwealth.

Independently Forecasted Component Unit (IFCU) operational expenditures: Most IFCU payroll and non-payroll expenses grow by inflation, with exceptions for certain expense categories (e.g., healthcare costs grow with medical inflation, variable costs that grow in line with revenues).

5.2.3 Other federal funding

Most federal funds received by the Commonwealth are passed through to residents directly in the form of social benefits (e.g., TANF, WIC), but federal funds are also used to cover operating expenditures in many agencies. The 2021 Fiscal Plan assumes federal fund inflows and outflows are forecast to mirror each other over time and are therefore surplus neutral to the Commonwealth.

5.2.4 Medicaid expenditures

Medicaid costs are projected to reach nearly \$6.5 billion annually by FY2025. These costs are primarily driven by the weighted-average cost per member per month (PMPM) multiplied by the estimated number of people enrolled in the Medicaid (federal and Commonwealth-qualified), CHIP, and Platino dual-eligible programs. Projections also include other direct health expenditures (e.g., Hepatitis C, HIV, and pulmonary programs) that do not flow through managed care. These costs are exclusive of non-medical administrative costs to ASES and the Department of Health. Given the long-term vision of state-like treatment, consistent with President Biden's commitment for providing Puerto Rico parity in Federal Funding Programs, the 2021 Fiscal Plan also includes incremental Medicaid costs on account of the long-term care and Medicare premium and cost share, which are currently not covered. These incremental Medicaid expenditures are critical towards achieving an improved and more affordable health system for Puerto Rico residents, and are forecast to reach approximately \$2.0 billion in new expenditures by FY2025.

Per Member per Month (PMPM) costs are forecast across 13 different Medicaid populations, such as Medicaid, CHIP, and Dual Eligible (Platino). PMPM rates can differ dramatically across such populations. For example, the Maternity population is forecast to have

a PMPM cost of over \$5,000/member/month in FY2021, whereas the Medicaid population is forecast to have only a \$218/member/month cost in FY2021. PMPM costs are projected to grow at the annual healthcare inflation growth rate of ~5.1% in FY2023 and beyond.

Enrollment rates, much like PMPM costs, are forecast across the 13 different Medicaid populations. These too range dramatically in size; for example, there are forecast to be only ~1,000 enrollees in the Maternity population, while the Medicaid population, which reflects the largest population on island, is forecast to have over 500,000 million individuals enrolled in FY2021. Growth in enrollment rates is primarily tied to the overall annual population decline for Puerto Rico. Additional changes in enrollment may be driven by the COVID-19 pandemic or other unexpected events.

EXHIBIT 18: PROJECTIONS FOR MEDICAID ENROLLMENT AND EXPENDITURES (\$M TOTAL COST, M ENROLLEES)



Other Commonwealth Non-Premium Medicaid expenditures, which include HIV programs and hospital reimbursement increases, among others, are projected to grow at the rate of Puerto Rico healthcare inflation. Separate from those costs is the Health Insurance Tax (HIT), calculated each year by the Federal Government and estimated here to be 1.80% of the prior year’s total premiums.³⁴ The Further Consolidated Appropriations Act, 2020 repealed the HIT requirement. Thus, the 2021 Fiscal Plan only reflects the estimated HIT fee anticipated to be required to be paid in FY2021 on FY2020 premium expenditures. Thereafter, the HIT fee is eliminated from projections.

Platino dual-eligible program expenditures were estimated using a consistent \$10 PMPM over FY2019-FY2024 representing payment for wrap-around services supplementing main Medicare coverage (from FY2024 onwards, this cost grows by the PMPM growth rate). Enrollment is projected to be affected similarly to Medicaid enrollment. Platino costs are expected to total nearly \$37 million by FY2025.

5.2.5 Commonwealth pension expenditures

Pension costs: Projections rely on demographic and actuarial estimations for Employees’ Retirement System (ERS), Teachers’ Retirement System (TRS), and Judiciary Retirement

³⁴ See Sec 4003 of FOURTH CONTINUING APPROPRIATIONS FOR FISCAL YEAR 2018 at <https://www.congress.gov/115/plaws/publ120/PLAW-115publ120.pdf>. Based on actuarial estimates provided by ASES.

System (JRS) populations and benefit obligations. From FY2021-FY2026, costs are projected to grow slowly but remain approximately \$2.3 billion per year. Since FY2018, pension benefits for all plans have been paid on a pay-as-you-go basis.

5.2.6 Appropriations

Municipalities: Municipal appropriations are projected to remain constant at ~\$132 million per year, which represents the amount included in the FY2021 budget. The 2021 Fiscal Plan assumes that there will be no further cuts to municipal appropriations.

University of Puerto Rico (UPR): UPR appropriations are projected to be ~\$560 million in FY2021, growing at inflation. The 2021 Fiscal Plan assumes that there will be no further cuts to UPR appropriations.

Highways and Transportation Authority (HTA): The Commonwealth provides HTA with an annual appropriation for capital expenditures and other costs. The 2021 Fiscal Plan provides that the HTA appropriation will be variable and set to cover HTA's forecasted annual deficits (after operating expenses and capital expenditures), as well as fund an "emergency reserve" account for the agency. The target size of the emergency reserve is initially set at ~\$250 million, in-line with best practices in other US jurisdictions and will be adjusted each year in order to keep pace with inflation. As a result, the 2021 Fiscal Plan includes an average annual appropriation of ~\$219 million over FY2021-FY2023, with ~\$51 million per year funding OpEx deficits, ~\$123 million per year funding CapEx deficits, and ~\$45 million per year funding the "emergency reserve." Thereafter, the annual appropriation is forecasted to decline as HTA operating surpluses are available to fund capital account deficits.

5.2.7 Other operating & capital expenditures

Utilities: The 2020 Fiscal Plan uses the estimated billings from PREPA and PRASA on an agency level, which are then projected to grow over the period of FY2021-FY2030 according to forecasted utility rates (and then according to inflation thereafter).

Insurance (PRIMAS): The Commonwealth bears costs related to insurance premiums (e.g., property insurance, liability insurance), which have increased from FY2018 to FY2020 due to Hurricanes Irma and Maria. Given the potential risk of future hurricanes, the baseline expenses related to insurance have been increased and are expected to grow at Puerto Rico inflation.

Capital expenditures: Centrally funded General Fund maintenance and capital expenditures of the Commonwealth (excluding PREPA, PRASA, HTA self-funded capital expenditures and one-time transfers) are expected to grow by inflation over time from a baseline of ~\$367 million in FY2021. In FY2021, ~\$59 million of the baseline expenses will be appropriated to HTA (as part of the total appropriations), with the remaining ~\$308 million for use by the Commonwealth.³⁵ HTA's capital expenditure funds will be used to support reconstruction, maintenance, traffic reduction, completion of the strategic network, and P3-related expenditures. Other General Fund capital expenditures will be allocated to priority projects. The 2021 Fiscal Plan includes annual Special Revenue Fund capital expenditures of \$50 million, growing at Puerto Rico inflation.

5.2.8 Reconstruction and restructuring related expenditures

Cost-share for disaster relief funding: Federal funds for FEMA's public assistance and hazard mitigation programs typically require a local match from the entity receiving them

³⁵ Beginning in FY2022, a portion of this unallocated general fund capital expenditures is assumed to be used to cover certain capital expenditure related initiatives included in the FY2022 Government budget submission.

(anywhere from 10-25% of funds). In the case of Puerto Rico, the 2021 Fiscal Plan projects that the Commonwealth will need to cover an estimated ~10% of federal public assistance funds. A portion of the Commonwealth and instrumentalities' cost-match expenditures are projected to be covered by CDBG funds from FY2020 to FY2032, which amounts to \$2.4 billion. Meanwhile, the 2021 Fiscal Plan maintains \$600 million (from FY2020 to FY2032) in reserve funds in case less CDBG funding is available than is currently projected. If these funds are unspent, they would accumulate and be utilized as part of an emergency reserve fund going forward.

Restructuring-related costs: Commonwealth restructuring-related expenditures are projected at \$402 million for the period FY2021 to FY2024, and are comprised of all professional fees, including those of the Unsecured Creditors' Committee, the Retiree Committee, the Government, and the Oversight Board. Additionally, the 2021 Fiscal Plan includes the cost of a banker fee as part of the plan of adjustment transaction which is estimated to be \$35 million in FY2021.³⁶ The estimate for professional fees in the 2019 Fiscal Plan was developed, in conjunction with the Oversight Board, by analyzing FY2018 and FY2019 run-rate billings based on available information and soliciting input from certain professionals. Fees were benchmarked versus comparable restructuring situations that yield an average professional-fee-to-funded-debt ratio of 2.08% relative to 1.68% projected for the Commonwealth. In total, for the period from FY2018 to FY2024, the restructuring-related expenditures projection in the 2021 Fiscal Plan continues to be ~\$1.1 billion (with minor change from the 2019 and 2020 Certified Fiscal Plans). The Oversight Board's operating costs will remain at \$58 million per year from FY2020 to FY2026.

EXHIBIT 19: PROJECTED PROFESSIONAL FEES RELATIVE TO OTHER MAJOR RESTRUCTURINGS

	Date filed	Outstanding debt, USD	Total fees and expenses, USD	Fees to funded debt, %
City of Detroit, Michigan	Jul. 2013	\$20,000,000,000	\$177,910,000	0.89%
Residential Capital, LLC	May 2012	\$15,000,000,000	\$409,321,308	2.73%
Sabine Oil & Gas Corp.	Jul. 2015	\$2,800,000,000	\$78,553,223	2.81%
Caesars Entertainment Operating Company	Jan. 2015	\$18,000,000,000	\$258,278,005	1.43%
Lehman Brothers Holdings Inc.	Sep. 2008	\$613,000,000,000	\$956,957,469	0.16%
Lyondell Chemical Company	Jan. 2009	\$22,000,000,000	\$205,932,292	0.94%
American Airlines	Nov. 2011	\$11,000,000,000	\$391,637,858	3.56%
Washington Mutual, Inc.	Sep. 2008	\$8,000,000,000	\$271,085,213	3.39%
Edison Mission Energy	Dec. 2012	\$5,000,000,000	\$96,244,628	1.92%
Energy Future Holdings Corp.	Apr. 2014	\$40,000,000,000	\$450,110,233	1.13%
Puerto Rico	2017	\$64,000,000,000	\$1,099,000,000	1.72%

Summary Statistics

Avg.	1.89%
Max	3.56%
Min	0.16%
Med	1.68%

➡ Puerto Rico involves added complexity as the largest public sector restructuring in the history of the United States

Note: Puerto Rico Fees includes ~\$35 million of banker fees due to Commonwealth Plan Adjustment transaction.

³⁶ This estimate assumes Banker fees will be 10 basis points of the estimated \$35 billion in claims.

Emergency reserve: The Commonwealth will build up an emergency reserve of \$1.3 billion, or ~2.0% of FY2018 GNP, by reserving \$130 million per year for 10 years, which started in FY2019. The methodology supporting this reserve is informed by guidance provided to other Caribbean islands by the International Monetary Fund in defining an adequate emergency reserve (2-4% of GNP, accumulated at 0.5% per year).³⁷ Restrictions on the use of this fund will ensure that it is a true emergency reserve. The 2021 Fiscal Plan includes the emergency reserve for \$130 million per year through FY2028.

³⁷ IMF Bahamas Article IV report published March 22, 2018.

Chapter 6. Long-term projections and Debt Sustainability Analysis (DSA)

While the 2021 Fiscal Plan emphasizes actions to be taken in the period from FY2021-FY2025, the Government's ultimate goal is long-term fiscal responsibility. As such, long-term projections are an important component in evaluating the 2021 Fiscal Plan's implementation and in the resulting Debt Sustainability Analysis (DSA). The outcome of the DSA pertains to traditional debt only, and not to other types such as contingent or no-default debt. Given large swings in debt sustainability shown in the sensitivity analysis, the amount of sustainable debt is contingent on several factors. Finally, the debt sustainability analysis should be adjusted going forward to account for new facts when available and errors when proven.

Consistent with the tenor of the new bonds contemplated as part of the February 2021 PSA which includes New Bonds from FY2022 – FY2046, the 2021 Fiscal Plan forecast through FY2046.

6.1 Long-term macroeconomic, revenue, and expenditure projections

While GNP trends are volatile in the short term due to COVID-19, as well as the impact of the hurricanes and earthquakes, real GNP growth in the latter part of the forecast period is negative and gradually declines as disaster relief funding drops off considerably and structural reform growth rates are muted. Nominal growth in the long-term settles at a rate of ~1.3%. The population is estimated to steadily decline at an average rate of ~1.2% annually, largely due to declining fertility rates. Inflation settles at a long-term run-rate of ~2.0% as it is expected to gradually converge to mainland forecasts.

Most revenues are projected to grow with nominal GNP in the long term.³⁸ This includes SUT, corporate income tax, personal income tax, non-resident withholding not paid by Act 154 entities and most General Fund revenues. Exceptions include:

- **Alcoholic beverages and cigarette-related tax revenues**, which are expected to grow by inflation and population. This assumption is supported both by relatively constant alcohol consumption in growing economies along with the long-term decline in cigarette consumption both in Puerto Rico and the U.S. mainland.
- **Rum excise on offshore shipments**, is expected to grow by U.S. mainland population and is partially driven by the statutory waterfall by which rum excise taxes are paid into the General Fund.
- **Non-resident withholding (NRW) and Act 154 revenues**, which will face declines due to US tax reform, supply chain diversification, and patent expirations. This decline had begun during FY2020, with incremental declines forecasted in each year through FY2023. No further declines are anticipated through FY2027; however, additional losses of Act 154 revenue are expected in FY2028-FY2031, such that FY2031 revenues are projected to be 64.4% below the 2018 baseline. This leads to a steady state of \$859 million in annual Act 154 revenues beginning in FY2031. NRW payments made by Act 154 payers are projected to follow a similar trajectory, though with a shallower decline.

³⁸ This methodology is consistent with general IMF forecasting approaches and is intended to capture the overall change in consumption, investment, and production within the economy.

- **Independently Forecasted Component Units (IFCU) revenues:** IFCU revenues are projected on a line-item basis and grow by the same values as in the short-term projections (largely by nominal GNP, with exceptions for those related to healthcare, population, or other factors). The only IFCU with a different short-term and long-term revenue projection is the State Insurance Fund Corporation, for which the Fiscal Plan projects an increase in revenues related to disaster recovery for FY2020-FY2032, reflecting the short-term increase in construction sector activity.

Federal fund revenues grow based on historical and statutory appropriations. **Medicaid** receives the most significant federal funding. In the long term, most federal fund revenues related to Medicaid, which mirror federal fund expenses related to Medicaid, grow at a rate of 5.1% offset by the forecast population decline, as outlined below in the “Medicaid Premium” section.

Just as most revenues grow by GNP, most **expenditures grow by standard inflation** after FY2025. Exceptions include:

- **Medicaid premiums** grow at a faster pace than standard inflation and are instead grown by a PMPM growth rate offset by the population change. PMPM costs for premium expenditures are projected to grow at an annual growth rate of 5.1% for the entirety of the forecast. This rate tracks pre-hurricane growth in Puerto Rico after the Island switched to a fully managed care model in 2015. The population change over the long-term averages ~-1.2% per year. Non-premium costs, such as administrative and payroll costs, grow by standard inflation in the long-term.
- **Capital expenditures** are anticipated to rise to 1.9% of GNP (in line with the mainland average) by FY2038, increasing the annual Commonwealth average to ~\$660 million over FY2038-FY2046, on average, as Puerto Rico must sustain a higher level of maintenance and rely on its own funding for capital investments (rather than disaster relief funding). **Cost match for disaster-related federal funding** increases from FY2026 to FY2032, as the Commonwealth pays the entirety of the cost match during that period. The Commonwealth is not responsible for the portion of funds allocated to instrumentalities (e.g., PREPA, PRASA, HTA).
- **Independently Forecasted Component Units (IFCU) expenditures** are forecast on a line-item basis. Most grow with standard Puerto Rico inflation with some exceptions, such as healthcare or claims related expenditures. Over the long-term, the expenses of healthcare related IFCUs (e.g., ASEM, Cardio) are projected to grow faster than revenues, creating a deficit. This Fiscal Plan assumes deficits related to healthcare will be funded by the Commonwealth.

Fiscal measures grow by their relevant macroeconomic indicator (e.g., revenues by nominal Puerto Rican GNP, expenditures by Puerto Rican inflation, healthcare measure by health inflation and population).

EXHIBIT 20: ANNUAL LONG-TERM FISCAL PLAN PROJECTIONS

Projections	FY2021	FY2025	FY2030	FY2035	FY2040	FY2046
Populations, Thousands	3,170	3,069	2,909	2,739	2,578	2,400
Population growth rate, %	-0.45%	-0.92%	-1.14%	-1.22%	-1.19%	-1.18%
Real GNP growth %	-3.57%	1.08%	-0.65%	-1.03%	-0.71%	-0.56%
Nominal GNP, \$M	67,800	75,747	78,690	79,232	84,007	91,175
Nominal GNP per capita, \$	21,387	24,682	27,052	28,929	32,587	37,990
Nominal GNP, per capita growth %	-2.45%	3.49%	2.05%	1.80%	2.51%	2.65%
Inflation, %	0.71%	1.44%	1.55%	1.60%	2.01%	2.01%
Disaster funding, \$M	7,202	8,128	3,429	-	-	-
Revenues, \$M	24,701	26,810	28,476	30,155	33,213	37,912
Commonwealth Revenues	15,804	14,975	14,989	14,766	15,474	16,726
Federal transfers	8,897	11,836	13,487	15,389	17,739	21,186
Expenditures, \$M	(23,084)	(25,497)	(27,453)	(30,000)	(33,426)	(38,080)
Commonwealth-funded expenditure	(13,330)	(12,703)	(12,937)	(13,505)	(14,478)	(15,538)
Federally-funded expenditures	(8,897)	(11,836)	(13,487)	(15,389)	(17,739)	(21,186)
Other Expenditures Outside of Budget	(858)	(958)	(1,029)	(1,106)	(1,209)	(1,357)
Gap / Surplus, \$M	1,617	1,313	1,023	154	(213)	(169)
Contractual debt service payments	-	(625)	(660)	(370)	(195)	(159)
Net gap / surplus, \$M	1,617	688	363	(216)	(408)	(328)

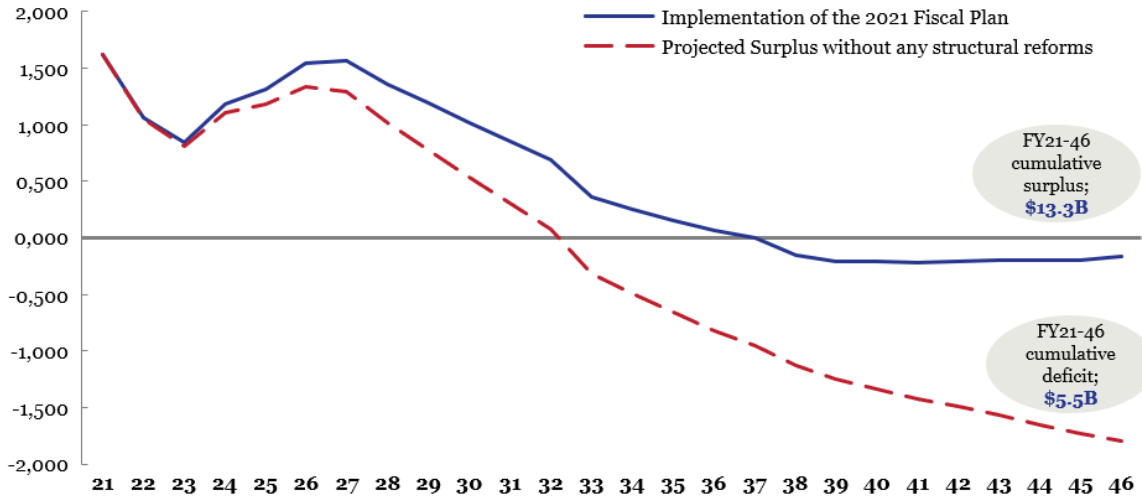
EXHIBIT 21: CUMULATIVE LONG-TERM FISCAL PLAN PROJECTIONS

#	Description	Ref	5-Year FY21-25	10-Year FY21-30	15-Year FY21-35	20-Year FY21-40	26-Year FY21-46
Revenues							
<u>General Fund Revenues</u>							
3.	Individual Income Taxes		8,940	17,798	26,545	35,560	47,196
4.	Corporate Income Taxes		8,838	17,394	25,452	33,694	44,375
5.	SUT Collections (General Fund)		11,056	22,598	33,594	44,378	58,440
6.	Act 154 Collections		6,647	12,133	16,427	20,720	25,873
7.	All Other General Fund Revenues	[a]	11,327	22,826	34,269	45,988	60,784
8.	Sub-Total, General Fund Revenues		46,809	92,749	136,286	180,340	236,669
<u>Other Revenues</u>							
10.	Tax Revenues & Other		11,048	22,522	34,238	46,393	61,868
11.	Component Unit Revenue		5,856	12,286	18,621	25,164	33,639
12.	SRF - Revenue and Medicaid	[c]	10,773	22,405	34,622	47,590	64,417
13.	Sub-Total, Other Revenues		27,677	57,212	87,481	119,147	159,924
14.	Total, Own Source Revenues		74,486	149,962	223,767	299,487	396,593
15.	Federal Transfers		54,290	118,326	191,348	275,111	393,278
16.	Total, Revenues		128,776	268,287	415,115	574,598	789,871
Expenses							
<u>General Fund Expenses</u>							
19.	General Fund - Payroll		(13,885)	(28,380)	(43,879)	(60,587)	(82,679)
20.	General Fund - Operating Expenses		(6,114)	(12,373)	(18,958)	(25,935)	(34,971)
21.	General Fund - Pensions		(10,327)	(20,516)	(30,488)	(39,802)	(49,259)
22.	General Fund - Medicaid		(2,553)	(5,985)	(10,123)	(15,104)	(22,451)
23.	General Fund - Other	[b]	(14,338)	(25,953)	(37,196)	(49,703)	(66,334)
24.	Sub-Total, General Fund Expenses		(47,217)	(93,208)	(140,644)	(191,131)	(255,694)
<u>Special Revenue Fund Expenses</u>							
26.	SRF - Component Unit Expenses		(5,902)	(12,135)	(18,697)	(25,789)	(35,183)
27.	SRF - Revenue and Medicaid	[c]	(10,750)	(22,315)	(34,428)	(47,244)	(63,811)
28.	Sub-Total, Special Revenue Fund Expenses		(16,652)	(34,450)	(53,125)	(73,033)	(98,994)
29.	Federal Fund Expenses		(54,290)	(118,326)	(191,348)	(275,111)	(393,278)
30.	Other Expenditures		(4,598)	(9,599)	(14,971)	(20,796)	(28,558)
31.	Total, Expenses		(122,757)	(255,583)	(400,088)	(560,071)	(776,524)
32.	Surplus/(Deficit) - Excl. Debt Payments		6,019	12,705	15,027	14,528	13,347
33.	Debt Service		(2,939)	(6,028)	(8,619)	(9,960)	(10,915)
34.	Surplus/(Deficit) - Incl. Debt Payments	[d]	3,080	6,676	6,408	4,568	2,432
<u>Memo: Medicaid Funding</u>							
36.	Medicaid - CW Funded		(2,553)	(5,985)	(10,123)	(15,104)	(22,451)
37.	Medicaid - SRF Funded		(1,670)	(3,698)	(6,140)	(9,073)	(13,394)
38.	Medicaid - Federally Funded		(23,487)	(54,483)	(91,847)	(136,797)	(203,059)
39.	Medicaid - Total Expenses		(27,710)	(64,166)	(108,110)	(160,974)	(238,904)
40.	<i>Medicaid - Implied Aggregate FMAP</i>		85%	85%	85%	85%	85%

Notes

- [a] Includes: Non-Resident Withholdings; Alcoholic Beverages; Cigarettes; Motor Vehicles and Excises on Off-Shore Shipment Rum.
[b] Includes: General Fund Capital Expenditures, Appropriations, COVID & Related Investments, Other Miscellaneous Items.
[c] Difference in SRF Agency Revenues and SRF Agency Expenses reflects impact of SRF Agency related right-sizing measures.
[d] Effective date disbursements on account of proposed plan of adjustment are not shown above and will be paid out of cash.

EXHIBIT 22: ANNUAL GAP/SURPLUS BASED ON IMPACT OF STRUCTURAL REFORMS (\$M)



6.2 Debt Sustainability Analysis (DSA)

The restructuring of the Commonwealth of Puerto Rico is a complex and on-going process involving multiple creditor groups, which has been further exacerbated by natural disasters and the spread of COVID-19. Material progress has been made to restructure Puerto Rico’s debt, as discussed in *Chapter 2*.

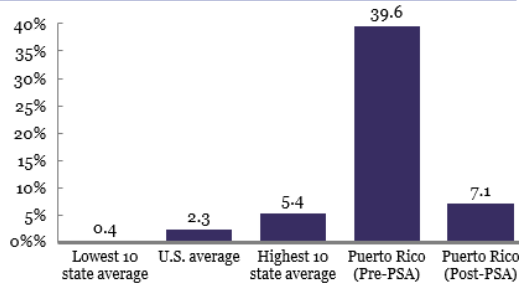
The DSA is intended to provide a framework for assessing the long-term capacity of the Government to pay debt service on its bonded debt. Debt levels post-restructuring need to be sustainable over the long-term and consistent with both a minimal risk of default on the restructured debt and a recovery of market access for future new money borrowings for ongoing infrastructure investment. The analysis begins with the 2021 Fiscal Plan and is then informed by the debt sustained by the most appropriate peer group against which to benchmark Puerto Rico. The DSA then applies rating agency metrics for that benchmark group to Puerto Rico to arrive at an assessment of what debt levels are sustainable in light of long-term projections and the peer metrics. Net tax-supported debt is defined as debt payable from statewide taxes and other general resources, net of obligations that are self-supporting from pledged sources other than state taxes or operating resources (such as utility or local government revenues). Prior to the enactment of PROMESA, Puerto Rico had approximately \$45 billion in tax-supported debt with a declining economy and no guarantee of sustained federal funding. Post-COFINA restructuring, Puerto Rico net tax supported debt outstanding was approximately \$41 billion, comprised of GO, PBA, COFINA, PRIFA, HTA, CCDA, ERS, Public Finance Corporation (PFC), and other intergovernmental loans. Net of the restructured COFINA debt, Puerto Rico’s other net tax-supported debt outstanding totals approximately \$28 billion. The below graphics additionally illustrate amounts contemplated as part of the February 2021 PSA³⁹.

³⁹ The February 2021 PSA reflects the current agreement between holders of General Obligation and Public Buildings Authority bonds and the Oversight Board. The February 2021 PSA is subject to incorporation in the Plan of adjustment and other definitive documentation and is shown herein for illustrative purposes.

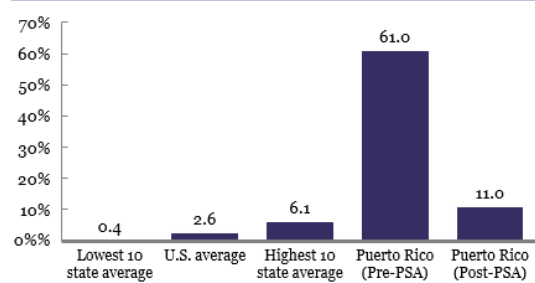
US states as peer comparables: Like US states, Puerto Rico does not control its own currency, has no access to IMF restructuring support programs or similar international sovereign relief funding packages and traditionally has been reliant on access to the same long-term municipal bond market used by the US states to finance their capital needs. Puerto Rico’s bonds are also rated by the same rating agency analyst groups that assign ratings to US states, not by foreign sovereign bond rating analysts. For these and other reasons, Puerto Rico has more similarities to US states than to sovereign nations. By virtually any measure tracked by the rating agencies, Puerto Rico’s existing debt levels, prior to the February 2021 PSA, are clear outliers relative to these US state peers.

EXHIBIT 23: US STATES AS COMPARABLES

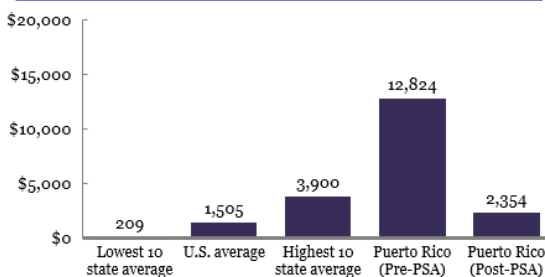
Net tax-supported debt, % of GDP



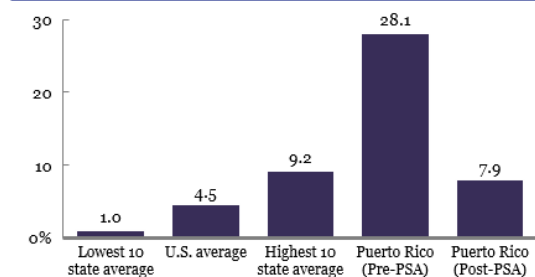
Net tax-supported debt to state personal income, %



Net tax-supported debt per capita, \$/person



Debt service, % of own-source revenues⁽¹⁾



(1) Own revenues includes all Commonwealth-collected revenues and excludes all federal transfers. Post-PSA reflects MADS cap excluding contingent value instrument and capital appreciation bonds. Post-PSA reflects FY22 revenues. Pre-PSA reflects amount per May 27th, 2020 Certified Fiscal Plan.

SOURCE: Moody’s investors service, “Medians – State debt declines in 2019, but likely to grow in coming years from May 12, 2020” NOTE: Puerto Rico benchmark metrics per Moody’s debt service as % of revenues based on 2022 own-source government revenues, personal income reflects FY22 preliminary estimates from Commonwealth.

Metrics for debt sustainability: Viewing US states as the most comparable group for benchmarking Puerto Rico, the DSA uses the debt ratio metrics in the “Medians – State debt declines in 2019, but likely to grow in coming years from May 12, 2020” and the “Medians – Pension and OPEB liabilities fell in Fiscal 2019 ahead of jump in 2020 from September 8, 2020”. The key debt ratios for the ten lowest indebted states, the 25 lowest indebted states, the 25 highest indebted states, the ten highest indebted states, and the mean for all US states are shown below.

EXHIBIT 24: KEY DEBT RATIOS FOR US STATES

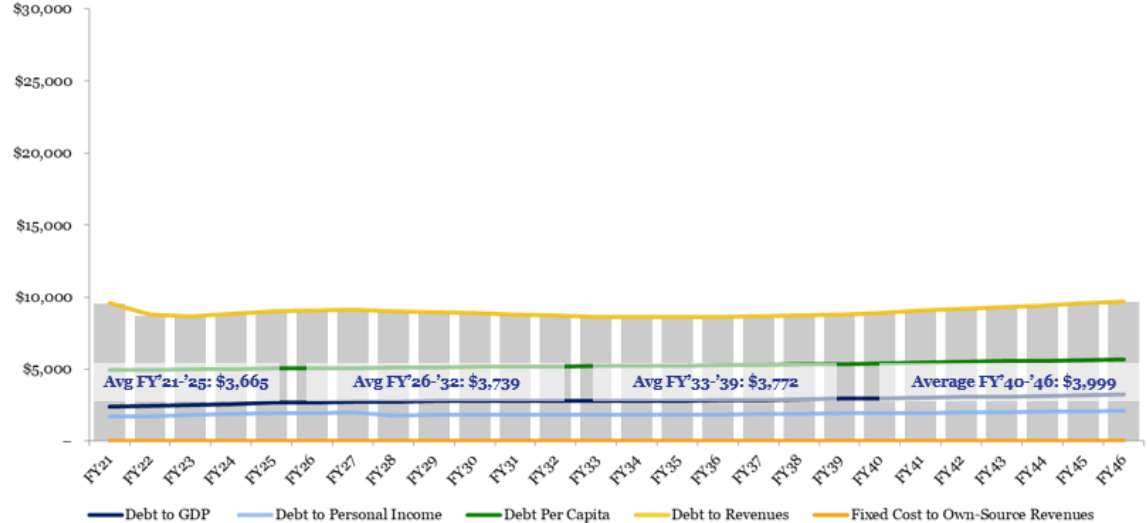
NTSD as a % of GDP ¹			NTSD as a % of Personal Income ¹			Debt per capita (U.S. dollar) ¹			Debt Service to Revenue ¹			Fixed Cost to Own-Source Revenues ²		
	Low 10	0.4%	Low 10	0.4%	Low 10	\$209	Low 10	0.9%	Low 10	3.3%		Low 10	3.3%	
	Low 25	0.9%	Low 25	1.0%	Low 25	\$500	Low 25	2.1%	Low 25	5.2%		Low 25	5.2%	
	Mean	2.3%	Mean	2.6%	Mean	\$1,505	Mean	4.3%	Mean	9.8%		Mean	9.8%	
	Top 25	3.8%	Top 25	4.2%	Top 25	\$2,511	Top 25	6.5%	Top 25	14.5%		Top 25	14.5%	
	Top 10	5.4%	Top 10	6.1%	Top 10	\$3,900	Top 10	9.2%	Top 10	21.2%		Top 10	21.2%	
1	Connecticut	8.3%	1	Hawaii	9.6%	1	Connecticut	\$6,637	1	Connecticut	14.7%	1	Illinois	32.9%
2	Hawaii	8.1%	2	Connecticut	8.4%	2	Massachusetts	\$6,258	2	Massachusetts	10.5%	2	Connecticut	29.8%
3	Massachusetts	7.2%	3	Massachusetts	8.3%	3	Hawaii	\$5,528	3	Illinois	9.9%	3	New Jersey	25.2%
4	New Jersey	5.7%	4	Delaware	6.1%	4	New Jersey	\$4,125	4	Hawaii	9.8%	4	Hawaii	24.7%
5	Mississippi	4.8%	5	New Jersey	5.8%	5	New York	\$3,314	5	New Jersey	9.6%	5	Kentucky	23.1%
6	Kentucky	4.7%	6	Kentucky	5.2%	6	Delaware	\$3,289	6	Kentucky	9.3%	6	Massachusetts	20.5%
7	Delaware	4.3%	7	Mississippi	4.8%	7	Illinois	\$2,625	7	New York	7.5%	7	Maryland	16.4%
8	West Virginia	3.9%	8	New York	4.6%	8	Washington	\$2,579	8	Washington	7.3%	8	Pennsylvania	13.7%
9	Rhode Island	3.9%	9	Illinois	4.5%	9	Maryland	\$2,323	9	Maryland	6.8%	9	Rhode Island	12.9%
10	New York	3.7%	10	Rhode Island	4.1%	10	Rhode Island	\$2,328	10	Mississippi	6.4%	10	Delaware	12.5%

1 Moody's investors service, "Medians – State debt declines in 2019, but likely to grow in coming years from May 12, 2020"

2 Moody's investors service, "Medians – Pension and OPEB liabilities fell in Fiscal 2019 ahead of jump in 2020 from September 8, 2020"

The analysis uses a long-term 26-year macroeconomic forecast to determine a range of implied debt capacity based on the debt and fixed cost metrics of the *average* US state. The debt capacity ranges shown are based off the following five methodologies: (i) debt to own-source revenues, (ii) debt per capita, (iii) debt to state personal income; (iv) debt to GDP; and (v) fixed costs to own-source revenues. Implied debt capacity and expected growth in debt capacity must be sufficient to cover both restructured debt and debt service on any future new money capital borrowings Puerto Rico needs to maintain its public infrastructure. To the extent new and additional revenues are enacted in the future, including revenues designed to support future capital projects or generated by public-private partnership infrastructure investments, then those initiatives could generate additional debt capacity for Puerto Rico that is not reflected in the current 2021 Fiscal Plan projections. Consistent with the February 2021 Commonwealth Plan Support Agreement, the debt service on Commonwealth tax-supported debt (excluding COFINA senior bonds) is limited to 25 years for the purposes of this analysis. Moody's defines "fixed costs" as the sum of a state's annual debt service and its annual budgetary pension and retiree healthcare (i.e., Other Post-Employment Benefits (OPEB)) expenditures. Given that Puerto Rico's public employee pension system is essentially zero percent funded – and that consequently the Central Government will pay pension expenditures on a fully PayGo basis from budgeted revenues each year – the fixed costs ratio helps capture that burden in comparison to the level of fixed costs as a percentage of Own Source Revenues for US States.

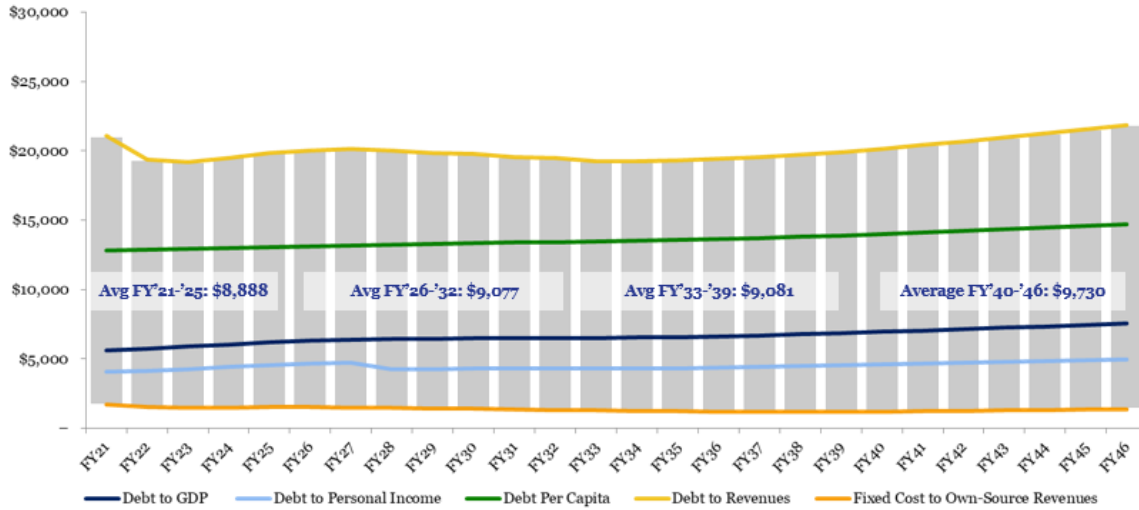
EXHIBIT 25: IMPLIED NET TAX-SUPPORTED DEBT CAPACITY RANGE BASED ON AVERAGE US STATE (\$M)



For illustration purposes; values in (\$000's)
 The Own Source Revenues metric used for the Debt Service and Fixed Costs measures includes the 53.65% Pledged Sales Tax Base Amount used to pay the restructured COFINA bonds, excludes restructured COFINA debt service to reach the implied debt capacity, and also excludes Federal Transfers. In all cases, future implied debt capacity range is limited to the Debt Service to Own Source Revenues Metric.

The DSA uses the long-term 26-year macroeconomic forecast to determine a range of implied debt capacity based on the debt metrics of the 10 highest indebted us states. The debt capacity ranges shown are based off the following five methodologies: (i) debt service to own source revenues, (ii) debt per capita, (iii) debt to state personal income, (iv) debt to GDP, and (v) fixed costs to own-source revenues. Implied debt capacity and expected growth in debt capacity must be sufficient to cover both restructured debt and future debt issuance.

EXHIBIT 26: IMPLIED NET TAX-SUPPORTED DEBT CAPACITY RANGE BASED ON TOP-10 HIGHEST INDEBTED US STATE DEBT METRICS (\$M)

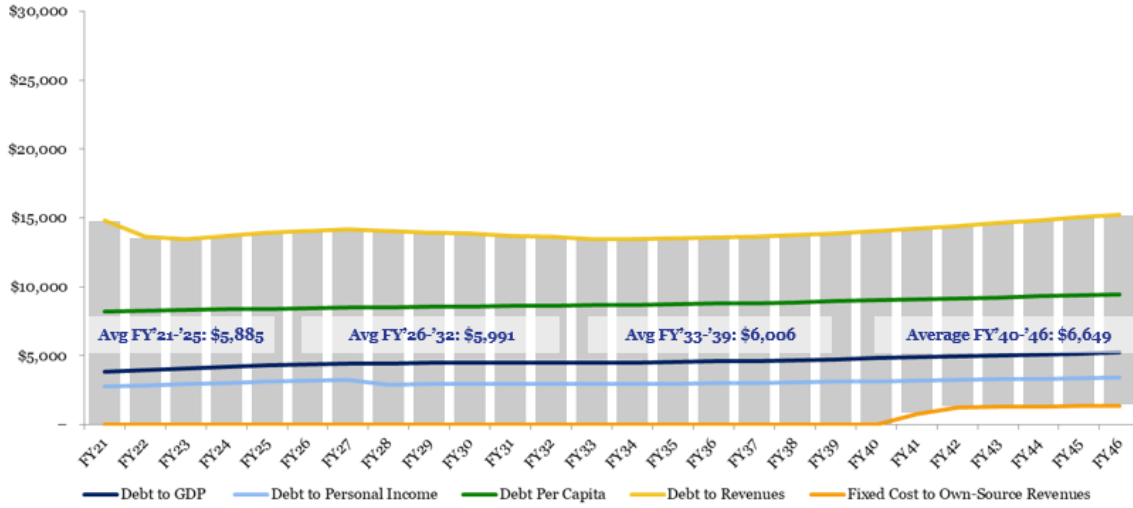


For illustration purposes; values in (\$000's)
 The Own Source Revenues metric used for the Debt Service and Fixed Costs measures includes the 53.65% Pledged Sales Tax Base Amount used to pay the restructured COFINA bonds, excludes restructured COFINA debt service to reach the implied debt capacity, and also excludes Federal Transfers. In all cases, future implied debt capacity range is limited to the Debt Service to Own Source Revenues Metric.

The illustrative implied levels of the Government’s restructured debt in the previous chart are calculated by applying the Net Tax Supported Debt ratios of the “top ten” US states (in terms of debt load) to Puerto Rico’s future projected GDP, population, and Own-Source Revenues.

The exhibit below uses the long-term 26-year macroeconomic forecast to determine a range of implied debt capacity based on the debt metrics of the 25 highest indebted US states with the same five methodologies.

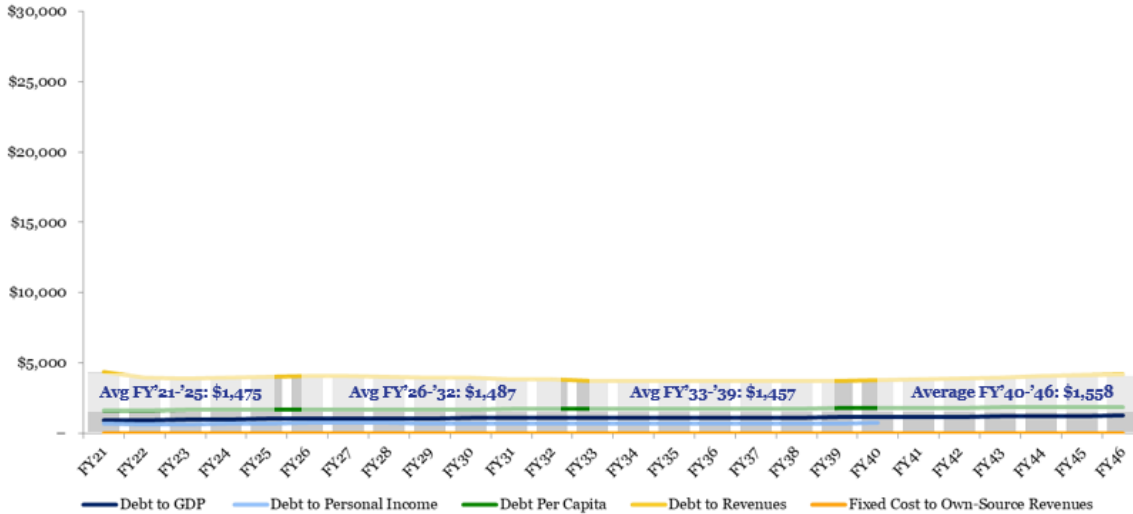
EXHIBIT 27: IMPLIED NET TAX-SUPPORTED DEBT CAPACITY RANGE BASED ON TOP-25 HIGHEST INDEBTED US STATE DEBT METRICS (\$M)



For illustration purposes, values in (\$000's)
 The Own Source Revenues metric used for the Debt Service and Fixed Costs measures includes the 53.65% Pledged Sales Tax Base Amount used to pay the restructured COFINA bonds, excludes restructured COFINA debt service to reach the implied debt capacity, and also excludes Federal Transfers. In all cases, future implied debt capacity range is limited to the Debt Service to Own Source Revenues Metric.

The exhibit below uses the long-term 26-year macroeconomic forecast to determine a range of implied debt capacity based on the debt metrics of the 25 lowest indebted US states with the same five methodologies.

EXHIBIT 28: IMPLIED NET TAX-SUPPORTED DEBT CAPACITY RANGE BASED ON 25 LOWEST INDEBTED US STATE DEBT METRICS (\$M)



For illustration purposes, values in (\$000's)
 The Own Source Revenues metric used for the Debt Service and Fixed Costs measures includes the 53.65% Pledged Sales Tax Base Amount used to pay the restructured COFINA bonds, excludes restructured COFINA debt service to reach the implied debt capacity, and also excludes Federal Transfers. In all cases, future implied debt capacity range is limited to the Debt Service to Own Source Revenues Metric.

Maximum annual debt service cap on restructured fixed payment debt: The implied debt capacity and expected growth in debt capacity must be sufficient to cover both the payments due on the restructured debt and all payments due on future new money borrowings. Accordingly, the aggregate debt service due on all fixed payment debt issued in the restructuring of the Government’s existing tax-supported debt should be capped at a MADS level. The cap would be derived from the US state rating metrics, and specifically from what Moody’s calls the “Debt Service Ratio.” The Debt Service Ratio is the ratio of total payments due in a year on all existing net tax-supported debt over that state government’s own-source revenues (i.e., excluding federal transfer payments) in that year.

The Moody’s report indicates that the average Debt Service Ratio for all US states is 4.3%. The Moody’s report indicates that the average Debt Service Ratio for the top 10 most indebted states is 9.2%. The Moody’s report indicates that the average Debt Service Ratio for the top 25 most indebted states is 6.5%. The Moody’s report indicates that the average Debt Service Ratio for the 25 lowest indebted states is 2.1%.

The February 2021 PSA includes a MADS cap of \$1.15 billion, which represents ~7.9% based on own source revenues included the 2021 Fiscal Plan⁴⁰. This debt service to own source revenue percent is between the average of the top 25 most indebted states and the top 10 most indebted states.

With respect to the Moody’s Fixed Costs Ratio, the September 2020 Moody’s report indicates that the average Fixed Costs Ratio for all US States is 9.8%. The same report indicates that the average Fixed Costs Ratio for the 10 States with the highest Fixed Costs Ratios is 21.2%, the average Fixed Costs Ratio for the 25 States with the highest Fixed Costs Ratios is 14.5%, and the average Fixed Costs Ratio for the 25 States with the lowest Fixed Costs Ratios is 5.2%.

Debt sustainability analysis: The below exhibit calculates implied debt capacity based on a range of interest rates and 2021 Fiscal Plan risk factors under an assumed illustrative 25-year term and level debt service. The risk factor is calculated by reducing the amount of projected cash flow available per year for debt service by a certain percentage. For example, a 20% risk factor case would use only 80% of the projected cash flow available to pay debt service on fixed payment debt.

EXHIBIT 29: IMPLIED DEBT CAPACITY BASED ON RANGE OF INTEREST RATES AND RISK FACTORS (\$M)

Illustrative Surplus Available		Implied Debt Capacity at Surplus				
		\$200	\$400	\$600	\$800	\$1,000
Sensitivity Analysis: PV Rate %	4.5%	2,373	4,745	7,118	9,490	11,863
	5.0%	2,255	4,510	6,765	9,020	11,275
	5.5%	2,146	4,292	6,439	8,585	10,731
Illustrative Surplus Available		Implied Debt Capacity at 5% PV Rate				
		\$200	\$400	\$600	\$800	\$1,000
Sensitivity Analysis: % Contingency	10.0%	2,669	5,338	8,007	10,676	13,345
	20.0%	2,373	4,745	7,118	9,490	11,863
	30.0%	2,076	4,152	6,228	8,304	10,380

⁴⁰ Excludes debt service on account of General Obligation Capital Appreciation Bonds. Additionally, reflects projected FY2022 revenues.

Restoration of cost-effective market access: As Puerto Rico seeks to regain cost-effective capital markets access, rating analysts and investors will demand that the Government demonstrate improvement in all four core areas of creditworthiness identified by Moody's: (i) the economy, (ii) Government finances, (iii) governance and "fixed cost" debt service, and (iv) pension expenditures. Together, these and other measures outlined in the 2021 Fiscal Plan can chart a path to restoring Puerto Rico's market access.

Part III: Federal Fund Parity

As a result of its territorial status, Puerto Rico has historically received inferior treatment in certain federal programs relative to U.S. jurisdictions. The below represent the population of programs under which Puerto Rico would receive additional federal support if it were at parity with states, or at least receive state-like treatment:

Medicaid: As discussed more comprehensively in *Chapter 12*, Puerto Rico and other territories receive piecemeal Medicaid support from the Federal Government. The lack of certainty surrounding federal funds has resulted in a depressed healthcare sector and a Medicaid platform that provides significantly less benefits to the people of Puerto Rico than their stateside peers. Under the formula used for states, Puerto Rico's largest population would receive an ~83% FMAP as compared to 55%, the island's statutory or standard rate. Additionally, the certainty of program funding would enable Puerto Rico to design and implement a platform that provides the same level of services received by stateside citizens.

Medicare: In fiscal year 2010, actual federal Medicare spending in Puerto Rico was \$4.5 billion; if Puerto Rico had been a state in calendar year 2010, estimated federal spending would have ranged from \$4.5 billion to \$6.0 billion. The Medicare estimates consider certain changes under the Patient Protection and Affordable Care Act occurring after 2010 that would reduce spending. Also, the Medicare estimates depend on the estimates for Medicaid, as some individuals are eligible for both programs.

Supplemental Social Security (SSI): In fiscal year 2011, actual federal spending for a similar program in Puerto Rico was \$24 million; if Puerto Rico residents would have been eligible for SSI, estimated federal spending would have ranged from \$1.5 billion to \$1.8 billion.

Supplemental Nutritional Assistance Program (SNAP): If Puerto Rico would have received parity treatment in calendar year 2011, residents would have been eligible for SNAP, and estimated federal spending would have ranged from \$1.7 billion to \$2.6 billion. One reason why the low end of the estimate range is less than actual spending is because participants' benefits would be reduced because of benefits received from SSI, for which Puerto Rico Residents would newly qualify⁴¹.

⁴¹ "Information on How Statehood Would Potentially Affect Selected Federal Programs and Revenue Sources" www.gao.gov/assets/670/661335.pdf.

PART IV. Revitalizing Puerto Rico

Chapter 7. Governor Pierluisi's Approach to an Effective Government

Governor Pierluisi began his term in January 2021 facing one of the most challenging periods in modern Puerto Rico history, as the COVID-19 pandemic continues to disrupt all aspects of daily life at a time when Puerto Rico is still reeling from the economic impacts of recent natural disasters, such as the 2017 hurricanes and 2020 earthquakes. The Government recognizes that it needs to redouble its efforts to be more efficient and responsive to the needs of the people that are already experiencing the hardships caused by economic stagnation dating back to 2006 and exacerbated by the Government's Title III proceedings under PROMESA. With this scenario as a backdrop, the Administration's principles will focus on transparency, responsiveness, efficiency, and execution. The Government program outlines several initiatives centered on economic development, government excellence, and quality of life.

7.1 Emergence from Title III Restructuring Proceedings as Exeditiously as Possible

Despite having made significant progress in restructuring more than \$22 billion of public bond debt through GDB's Title VI Qualifying Modification and COFINA's Title III Plan of Adjustment, the Commonwealth still remains in a costly in-court restructuring proceeding. Governor Pierluisi has emphasized that a primary goal of his administration is for the Commonwealth to emerge from its Title III proceedings as expeditiously and efficiently as possible. The path forward is to quickly complete these proceedings to save significant professional fees and accelerate the termination of the Oversight Board, all of which will enhance Puerto Rico's reentry into the capital markets.

7.2 Economic Development

As the Government continues to work with the Oversight Board to emerge from its Title III cases, Governor Pierluisi's administration recognizes that—beyond restructuring its bond debt—garnering public trust in Puerto Rico's leaders and institutions must be the cornerstone for long-term economic development on the Island.

After nearly two decades of economic depression, Puerto Rico has been plunged into insolvency and a complex process of fiscal oversight and debt restructuring, mixed with historic natural disasters and a pandemic. The result of this economic contraction has led to a notable deterioration in the public sector, in the capacity to finance and modernize Puerto Rico's infrastructure, and in the quality of public services. In the private sector, it has caused a loss of wealth, a rise in bankruptcies and a smaller market as Puerto Rico residents move to the U.S mainland jurisdictions. For decades, Puerto Rico has also seen its credibility in the Federal Government and in the capital and investment markets tainted by acts of corruption and the constant change in the laws and regulations for doing business on the Island. But it is the people's loss of confidence in their government leaders and institutions that is of greatest concern and must be addressed as a priority. It will take cross-sector and cross-functional collaboration to return to a path of growth, to rescue Puerto Rico's credibility, provide citizens with a government that executes, and establish a good investment climate that will create jobs in Puerto Rico:

- The recovery and rebuilding of Puerto Rico are priorities for Puerto Rico's development and resilience. To successfully achieve the reconstruction of the Island, direct funding from FEMA's public assistance and mitigation programs and the CDBG-DR program must be expedited and maximized, in addition to the billions of dollars approved under the CARES Act and other federal COVID-19 stimulus funds. This will address the challenges of pandemics, earthquakes and hurricanes and provide an immediate boost to the local economy while modernizing the local infrastructure.
- Short-term opportunities for competitive advantage focus on two main initiatives. The first, biopharma and medical device manufacturing to address COVID-19 and expand industrial operations under the initiatives *Manufacturing Reshoring and Bring Manufacturing Back*. The second, Puerto Rico as an international air cargo and passenger transshipment hub in the region, after achieving the important exemption from air cargo and passenger transshipment restrictions approved by the Federal Department of Transportation.
- Ease of doing business structural reforms and initiatives are aimed at improving the ease of doing business and the investment climate to increase the productivity and competitiveness of Puerto Rico and its businesses. These measures will also help small and medium-sized businesses, which cannot cope with the costs of government bureaucracy and inefficiency. Some of these initiatives include simplification and digitization of paperwork and permits, reduction in operating costs, such as energy and taxes on businesses, increased labor participation and productivity, and innovation and technological transformation.
- Strengthening of local commerce and industry by implementing the structural and targeted reforms necessary to facilitate doing business in Puerto Rico and increasing productivity and competitiveness. Priority and support should be given to SMEs following the impact of the COVID-19 pandemic through business training, seed funds for start-up companies and women entrepreneurs, telecommunications infrastructure for greater interconnectivity and technological access, buy "Local" and "Made in PR" campaigns, expansion of family agricultural markets, craft fairs (after COVID-19), promotion of exports of products from Puerto Rico, promotion of the collaborative economy and emerging industries.
- In keeping with the proposed creation of a human capital and labor force growth policy, it is necessary to implement timely complementary strategies to retain those who live on the Island, attract back those who have moved away, and embrace those who decide to relocate to Puerto Rico. Some of the proposed initiatives include a scholarship program, establishment of a fund for first employment, and promote Puerto Rico as a destination for Latin America investors.
- To empower local industry and promote investment, the Government will undertake efforts to substantially improve the ease of doing business on the Island by simplifying the complicated permitting and tax system, reducing government costs and burdens on business competitiveness, and expanding broadband infrastructure and telecommunications technology (5G technology and new technologies) for greater interconnectivity for citizens and businesses. Other opportunities are through the integrated investment promotion by InvestPR, effective use of investment promotion tools with the Incentive Code, Opportunity Zones Program, HUB Zones, EB-5 Programs, among others. It is also important to support strategic and emerging sectors such as robotics, alternative and renewable energy, aerospace and aeronautics, artificial intelligence, IoT, 5G, Smart Cities, cybersecurity, film and digital production, agricultural biotechnology, eSports and eGaming, blockchain, recycling and bioeconomy, fintech, 3D printing, design, and creative industries. The integrated development of science, technology and innovation will bring Puerto Rico closer to a knowledge-based economy and leverage local biopharma and medical device manufacturing industry and the technology and innovation sectors. Training young people in the subjects of science, technology, engineering, art, and mathematics (STEAM) is vital to prepare them for

the job and business needs of the present and future. The high level of specialization in STEAM generates the human capital necessary to implement public policy in science and technology.

- Promote the expansion of federally regulated industries such as aerospace and aeronautics, space exploration, defense manufacturing, federal contracting, and cybersecurity. Puerto Rico competes favorably in these sectors because it is part of the United States, because of its strategic geographic position, and because of its highly skilled human capital. Take advantage of the Puerto Rico Air Hub Strategy, among other initiatives for the development of the aerospace cluster, as well as the supporting supply chain.
- Stabilize agricultural production, historically affected by weather events typical of local climate and other economic factors such as price fluctuations of imported inputs. It is imperative to assist farmers in reducing their production costs and to increase the use of technology to achieve consistency in production, quality, and price.
- The energy sector has become an important industry in Puerto Rico through the adoption of renewable energy sources. Multiple professionals specializing in different functions work in this sector, representing an important segment of the economy which the government should facilitate its operation and growth.
- The manufacturing sector will be enhanced to retain, diversify, and expand its investments, operations, and jobs. This can be accomplished through the ease of doing business initiatives and reforms, modernization of infrastructure, investment promotion, high-technology and advanced manufacturing and competitive advantage.
- Tourism is one of the industries that has suffered the most due to the COVID-19 pandemic. Puerto Rico has great potential to expand the development of sustainable tourism, the integration of digital platforms, the collaborative economy, non-traditional hotels, ecotourism, and medical, sports and adventure, cultural, and gastronomic tourism, among others. Puerto Rico will capitalize on existing infrastructure to continue to expand and become a regional leader in group and convention tourism, as is the Convention Center District and the entire tourist area of the San Juan metropolitan area.
- Focus on developing, strengthening, and modernizing Puerto Rico's critical infrastructure with the goal of meeting the needs of the people of Puerto Rico. This can be accomplished by expediting funds and recovery projects, development of an infrastructure plan for Puerto Rico, simplifying and promoting public-private partnerships (P3s), simplification and digitalization of procedures and permits, development of a skilled construction workforce, and integration of local contractors, suppliers, and professionals. Attention should be paid to each of the components of Puerto Rico's critical infrastructure in order to modernize and strengthen them in accordance with existing resources, including recovery funds. These sectors include energy, health, transportation and highways, security, education, telecommunications, solid waste, ports and coasts, drinking water, sewage, banking, and finance.
- Key strategic projects will be prioritized in the identification of available support funds and will benefit from a streamlined permitting process overseen by the Governor's Office. Some of these projects include revitalization of urban centers affected by the hurricanes and earthquakes, new trauma hospital in Río Piedras and expansion of the Trauma Center in Mayagüez, redevelopment of Roosevelt Roads, Air Hub Strategy for air transshipment and air cargo hubs and sustainable economic development for Vieques and Culebra.
- Positioning Puerto Rico as a regional leader in services, manufacturing, technology, tourism, logistics, transportation and tourism sectors, becoming a hub for Latin American companies that use the Island as a platform for the U.S. mainland market.

- Simple and functional permit system that facilitates economic activity to build, expand and create new businesses, while complying with the safety of the population and taking measures for environmental protection, is crucial to return to growth. The areas to focus on are (i) business permits, for the establishment and renovation of businesses; and (ii) construction permits, for the construction and development of infrastructure, facilities of all types, and residences.

7.3 Government of Excellence

Adopting a new form of governance focused on excellence, execution, and transparency through which it can provide a better quality of service to the people of Puerto Rico is a priority of this Administration.

To achieve this, the Governor proposes empowering public workers by providing proper compensation and training resources and integrating them into the executive branch agenda. Personnel should be recruited based on merit, placing importance on relevant knowledge and skills needed to carry out the agency's mission and relevant functions. Agency resources should be effectively managed and civil service competencies should be strengthened through knowledge sharing initiatives that guarantee the continuity of services.

The Classification and Remuneration Plan will establish scales that reflect and guarantee the principle of equal pay for equal work and serves as a basis for evaluating employee performance. The plan proposed by this Administration is a step toward improving the working conditions of public employees, and therefore deserves to be evaluated as part of the necessary restructuring of the Government. The plan proposes to update the compensation of public employees in positions that have not been reviewed, in some cases, for decades. The plan is projected to impact 65 agencies and 8,539 employees (39% of total employees). This Administration places high importance on transparency and started off right with the coverage afforded to the transition hearings, allowing turns for questions and answers to the press, the public, relevant sectors of interest and creating a virtual repository with all documents exchanges. To continue this trend of transparency, the Government will offer access to information and will develop technologic capabilities to automate and digitize processes and documents. The contracting process will be reformed to ensure greater transparency, and the evaluation process should be agile and clear regarding the defined terms for evaluation and approval.

The focus of the government should be execution and service centered on the citizen. The barriers that prevent government from modernizing must be removed and replaced with innovation and digital transformation as a guiding principle for efficient and modern government. To address this, the following are some examples of proposed initiatives:

- Develop the critical infrastructure to enable the digital transformation of Puerto Rico and government operations as a tool to improve services, achieve greater resilience, maximize efficiencies, and reduce expenses
- Establish the corresponding framework to achieve interoperability and intercommunication among the government's various technology platforms, such as procurement, accounting, statistics and permitting systems
- Provide PRITS with the necessary authority and resources to carry out its mission to achieve digital transformation in government and implement a coordinated inter- and intra-agency policy
- Expand the use of the 311 system as an alternate citizen service channel for guidance on government procedures and services and for use by government agencies as call centers

- Create the Electronic Identity Online Access System (IDEAL) for individuals and businesses to be able to make government transactions and contracts without the need to submit government documents, emulating the best practices of countries such as South Korea, Denmark, and Estonia
- Municipal support is also critical, to ensure the continuity of essential services, solvency, and fiscal viability

The Government needs to finish restructuring Puerto Rico's debt in an efficient and fair manner and be fiscally responsible to terminate the FOMB as soon as possible. The Government will support an audit of the debt lead by the Comptroller's Office of Puerto Rico with the input of experts and union and civic leaders. The Government will also grant priority and resources for the timely delivery of the audited financial statements of the government and public corporations. To achieve greater fiscal responsibility, the government proposes simplifying compliance with tax obligations, use technology for tax procedures, strengthening the Treasury department, combating tax evasion, reducing the tax burden on individuals and businesses, supporting the growth of manufacturing in Puerto Rico, evaluating options to Act 154, and creating the Office of the Chief Financial Officer.

7.4 Quality of Life

A government guarantees a good quality of life when it provides all its citizens with the tools to progress, especially historically marginalized groups.

This Administration's mission is to make Puerto Rico a place where every resident lives the quality of life he or she deserves. The foundations of a good quality of life consist of a good health care system that is affordable, agile and of quality, a public education of excellence in preschool, K-12, and higher education (college, vocational, and technical), a society safe from crime and natural events, a community that highlights the civil rights and equality of its members and an ecosystem of respect for the environment and protection of natural resources.

Recent events, such as Hurricanes Irma and Maria, the earthquakes affecting the Island since December 2019, and the COVID-19 pandemic, have highlighted the deficiencies and inequities in the Puerto Rico health system. Following recent federal funding allocations, the biggest problem in health care has been the lack of action and efficient use of state and federal resources. This Administration will prioritize the use of those funds for the benefit of patients and health care providers.

The preparation, planning and effective implementation of a COVID-19 response covers matters related to testing, contact tracing, vaccination, changes in the structure of the Department of Health to address COVID-19 and other pandemics, and coordination between Department of Health and Department of Education for schools reopening. To achieve its objectives regarding the transformation of the health sector, the Governor's platform outlines a program that is based on the following priorities: (i) focus on the patient, (ii) strengthen and help local health care providers, (iii) modernize the infrastructure, (iv) interoperability and integration of health systems and other agencies, (v) a health system that encourages quality of services, being agile and effective, (vi) establish and abide by the highest standards of integrity, ethics and compliance.

It is the duty of the Department of Education and its various components to provide the necessary tools to equip students with the knowledge, disciplines, and educational experiences to become productive members of society. The Governor proposes educational strategies that are centered on empowering school principals and school teachers, decentralizing the Department of Education to bring it closer to school communities and empowering school

principals to guide them, investing in technology infrastructure to ensure education and data collection, especially in times of pandemics and emergencies, and modernize it to current times, improve the academic performance of students, and strengthening the University of Puerto Rico without additional cuts and providing it with the autonomy it requires.

The Government has an obligation to maintain a safe environment for every person residing in or visiting Puerto Rico. This Administration will implement a Comprehensive Security Plan, leading strategies and working in a transparent and coordinated manner with communities, municipalities, and state and federal governments. The Governor will responsibly address the challenges and take advantage of the opportunities to improve the system with the reform of the Puerto Rico Police, the allocation of fiscal resources, effective emergency response and management, evaluation of the Department of Public Safety and rehabilitation of the Department of Corrections.

It is imperative to guarantee the safety and working conditions of law enforcement officers and members of the Puerto Rico Police, and they must be adequately compensated and paid on time for overtime hours worked. The Government will urgently address the processes related to the retirement of local police officers and reiterates the commitment to zero cuts to their pensions. The Government will protect police officers who did not contribute to Social Security in the past and, therefore, do not have that supplement for their retirement. Additionally, the Government will seek alternatives so that every retired officer has access to a medical plan that meets his or her needs, including access to the VITAL Plan.

Additional measures aimed at improving the quality of life of the people of Puerto Rico include:

- Promote the strengthening of the Puerto Rico family integrity, minors, and youth
- Promote women's economic equality, and address gender violence through the declaration of a State of Emergency
- Help and care for older adults, who may be victims of poverty, lack of education, accessibility to services, fragmentation of the system, adaptation to the transition from productivity to retirement and relocation, social isolation, exploitation, mistreatment, stereotypes, dependency and lack of knowledge and prejudice about their contributions and capabilities
- No implementation of pension cuts for retirees, and will support measures to establish a fair pension of at least 50% of the retired public employee's salary
- Provide people with disabilities access to necessary resources, becoming a catalyst for the development of their potential, ensuring access to resources at different stages of their lives
- Take direct action to address the homelessness situation and help those that find themselves in a social and economic disadvantage
- Support and recognize the sacrifice, patriotism and bravery of veterans, ensuring optimal services in health and nutrition, vocational rehabilitation, education and training, job search, retirement planning strategies, community integration, self-care, and independence skills, including awareness and application for earned benefits tailored to their particular needs
- Implement coherent action plans that stimulate the participation of nonprofit organizations in the processes related to matters that affect the socioeconomic development of Puerto Rico, from the perspective of a "New Social Contract". The participation of municipal governments is a fundamental component in the development of alliances with organizations in their region and in the development of strategic community development plans and in the collaboration for the implementation of these plans

- Establish parallel measures to ensure the protection of Puerto Rico’s natural resources while promoting their responsible enjoyment and use, paying particular attention to achieving environmental justice in low-income communities who are disproportionately impacted by air pollution and protect the air quality and water supply

7.5 Broadband infrastructure

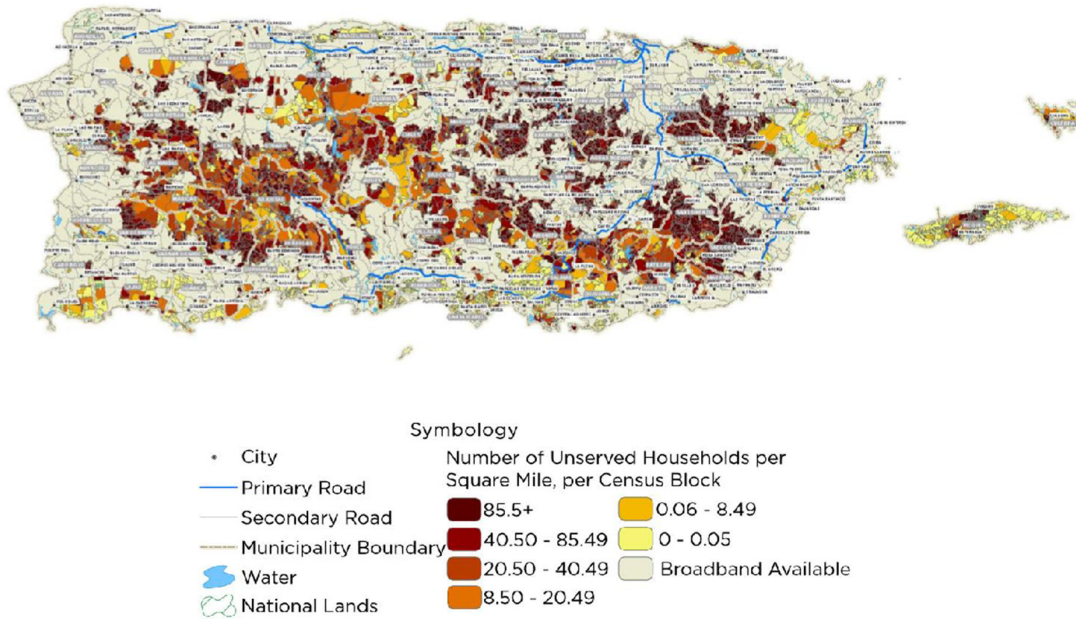
The 2012 Puerto Rico Broadband Strategic Plan (written by Connect Puerto Rico, in conjunction with the Puerto Rico Telecommunications Regulatory Board and Puerto Rico Broadband Taskforce) established a vision of a Puerto Rico with fast, robust, redundant, and ubiquitous broadband access. Broadband provides numerous socio-economic benefits to communities and individuals, including improving labor market outcomes by enabling remote education, increasing business productivity through better connectivity, providing access to better health care through telemedicine for those in rural areas, and enhancing civic participation through better access to information.

During the recent COVID-19 pandemic, internet access has become even more important to residents’ livelihoods. Across the US, telemedicine is becoming more widespread as a way to deliver health services safely. As public and private school systems alike move to distance learning models, students who do not have access to reliable, high speed internet are unable to participate – and therefore fall farther behind.

Unfortunately, within Puerto Rico, while there was some growth in broadband deployment in 2011-2014 (driven by an aggressive capacity upgrade of cable networks, as well as the deployment of fiber by other broadband providers), critical broadband infrastructure gaps still exist, particularly across rural areas of the Island. As of 2014 (the most recent year for which data is available), while ~99% of urban households across Puerto Rico had access to speeds of at least 10 Mbps download and 1.5 Mbps upload, this was true for only ~66% of rural households.⁴² Broadband adoption figures across Puerto Rico also reveal a persistent gap among certain demographic groups. Broadband non-adopters in Puerto Rico were generally low-income groups, senior citizens, people with disabilities, and/or individuals with less education, which mirrors demographic trends on the US mainland and elsewhere. These gaps have possibly widened since Hurricane Maria, particularly in the mountainous region of Puerto Rico, where topography has hindered replacement of damaged infrastructure.

⁴² Puerto Rico Broadband Strategic Assessment, 2015.

EXHIBIT 30: PUERTO RICO BROADBAND STRATEGIC ASESMENT (2015) – UNSERVED HOUSEHOLDS



Addressing the digital divide is critical to ensuring that all residents of Puerto Rico can take advantage of the many well well-documented socio-economic benefits afforded by Internet connections. These benefits are most evident when people have access to the Internet at speeds fast enough to be considered broadband; these speeds are required to facilitate full interaction with advanced online platforms.

In the private sector, expanding broadband infrastructure and telecommunications technology (5G technology and new technologies) for greater interconnectivity for citizens and businesses for the development of technological solutions under the Internet of Things (IoT), and for the development of so-called Smart Cities, where companies can interconnect with government assets or databases, or open in the network, to provide services and products at the level of the citizen and public benefit.

A successful broadband program will require strong leadership, accountability, continuity, and willingness to work with a broad range of entities, both within the Government and the private sector. While many similarities exist across state broadband programs and the activities that they are undertaking to close gaps in access, notable differences are also evident. These include the form and structure of the program, its life span, and the resources that the state has committed.

Some states, including Minnesota and Colorado, have broadband offices established by statute or executive order. Others, including Tennessee, have staff within an agency dedicated to supporting broadband programs.

The 2020 Fiscal Plan required AAFAF to conduct a transparent, competitive procurement process as reviewed and approved by the Oversight Board to select an organization to serve as the administrator of these funds (the “Fund Administrator”). The selected Fund Administrator must have a staff of experienced professionals and a dynamic network of collaborators that include a broad range of private and government organizations. The Fund Administrator must

also ensure accountability by requiring that all grantees demonstrate they are providing the service they were funded to deliver, while also providing the data needed to evaluate the program and progress toward defined goals. AAFAF issued an RFP for the Broadband Infrastructure Grant Administrator in October 2020 and is in process of completing procurement.

EXHIBIT 31: ALLOCATION OF STRATEGIC INVESTMENT FUNDING FOR TELECOM BROADBAND INFRASTRUCTURE (\$M)

Category	FY21	FY22	FY23	Total
Assessment – Update Plan	1.0	-	0.5	1.5
Broadband Grant Program	50.0	168.0	173.0	391.0
Trust Admin/Program Evaluation	2.5	2.5	2.5	7.5
Total	53.5	170.5	176.0	400.0

Over the next three years, in partnership with the Federal Government and both public and private stakeholders, the Fund Administrator must collaborate to assess, evaluate, and map various opportunities for broadband expansion. Broadband inventory maps and technology assessment research will enable a better understanding of the Puerto Rico broadband market and help define infrastructure needs in underserved regions, as well as ensure that money is sent to the right places. The Fund Administrator, in collaboration with the broadband provider community, information and communication technology providers, K-12 education stakeholders, the higher-education community, healthcare professionals, local government, grassroots community groups working to address the digital divide in their communities, and private sector groups for whom broadband is an essential investment asset, will be responsible for:

- Monitoring, measuring, and assessing the impact of broadband across the Puerto Rico economy
- Measuring and publishing aggregate, industry-wide data regarding broadband investment trends
- Measuring and publishing aggregate broadband use patterns
- Adjusting Puerto Rico economic indicators to estimate and monitor the impact broadband has on the overall economy

The Fund Administrator is tasked with developing a solicited proposal mechanism with the goal of providing funding to telecommunications operators and other Internet Service Providers to support broadband deployment in unserved and underserved areas. The Fund Administrator must institute grant reporting, data collection, and other accountability measures to ensure that funded projects deliver the promised service and provide data necessary for the state to evaluate progress toward its goals.

The Fund Administrator must ensure it leverages federal support for broadband expansion, by working to provide timely information and strategic planning support to broadband providers who can leverage FCC funding opportunities. The Fund Administrator, in collaboration with the Puerto Rico Broadband Taskforce, must also work to streamline construction permitting and planning and leverage existing public assets, such as poles, ducts, conduits, and rights-of-ways, to incentivize private broadband investments.

Through driving measuring, monitoring and strategic function to telecoms and internet service providers, the 2021 Fiscal Plan expects to improve the overall infrastructure on Island and to provide enhanced opportunities—through better and more equal access to education, healthcare, and information—for the people of Puerto Rico.

Chapter 8. Reinvestments

As described in *Chapter 7*, the 2021 Fiscal Plan includes a series of critical investments and initiatives asserted by Governor Pierluisi's administration that are vital toward Puerto Rico's future success.

With the onset of the COVID-19 pandemic and resulting economic damage, it is now more important than ever that the Government make the short-and long-term investments required to lay the groundwork for recovery and future innovation. The 2021 Fiscal Plan preserves investments included in 2020 Certified Fiscal Plan and supplements these initiatives with a series of investments that are imperative to Governor Pierluisi's administration. A summary of key investments in the 2021 Fiscal Plan are highlighted below.

8.1 Critical Investments Introduced in FY2020

- **Immediate response to COVID-19:** In response to COVID-19, the Government has worked closely with the Oversight Board to provide incremental investment to mitigate the effects of the COVID-19 economic shock, largely through the ongoing implementation of the local \$787 million Emergency Measures Support Package.
- **Investing in critical healthcare infrastructure:** The Government is addressing the need for infrastructure development that are necessary to serve people in underserved areas and address the gap to meet Puerto Rico's healthcare needs.
- **Enhancing healthcare services:** Healthcare continues to be a priority for the Government, particularly in light of the Island's recent history of natural disasters. Accordingly, the 2021 Fiscal Plan both preserves and supplements the strategic healthcare investments included in prior fiscal plans.
- **Safeguarding public safety:** The Government continues to prioritize public safety and include multi-year investments across all public safety agencies, with a focus on increased police compensation.
- **Driving educational outcomes:** Improving educational outcomes is an imperative, evidenced by a multi-year investment program above and beyond the substantial federal funds available to the Government. This includes investments in public school nurses and psychiatrists as well as additional teacher and school director compensation, amongst others.
- **Strengthening the technology sector:** To ensure Puerto Rico can compete in a global economy, the 2021 Fiscal Plan includes critical funds for technology infrastructure, such as broadband infrastructure and telecommunications technology.
- **Working Capital Fund:** To advance funds in the form of one or more loans, extensions of credit, or advances to central government agencies, public corporations and municipalities as a bridge to receipt of funding under FEMA programs to allow permanent recovery projects funded by FEMA programs to commence sooner than otherwise possible to help and expedite economic recovery. The Disaster Aid Revolving Fund will be used to advance the

Federal Share of funds reimbursable for permanent work projects which are fully obligated under FEMA's public assistance program and HMGP projects for incurred damages as a result of Hurricane Maria, Hurricane Irma, or the earthquakes declared in January 2020. This liquidity would allow recovery projects to start earlier than otherwise possible and proceed where the FEMA funding reimbursement process is slower than expected⁴³.

8.2 Municipalities and the University of Puerto Rico

No more Cuts to the Municipalities (\$44 million – Recurring): No additional reductions to transfers to municipalities, by establishing the current transfer of \$132 million as a base minimum to guarantee continued citizen access to local services. The Government supports and promotes shared service agreements and consortiums to consolidate municipal services.

No more Cuts to the University of Puerto Rico (\$94 million – Recurring): No additional reductions to state fund appropriation to the University of Puerto Rico, establishing the current contribution of \$560 million as a base minimum, to support the public university system as a critical contributor to the economic and social development of Puerto Rico.

8.3 Municipalities Health Plan Exemption Contribution

Elimination of Municipal Plan Vital Contributions (~\$162 million – Recurring): Municipalities deliver accessible and affordable public services such as health, sanitation, and emergency services. In recent years, many municipalities have been facing financial distress due to unforeseen disaster relief spending, payment of PayGo liabilities on account of Act 106-2017 and debt service payments. Such distress burdens the municipalities' day-to-day functions, which has a resulting negative impact on the critical services that they provide.

In February 2021, Governor Pierluisi signed a collaboration agreement with the New Progressive Party Mayors Federation and the Popular Democratic Party Mayors Association, in which the Administration committed to identifying resources to exempt municipalities from having to contribute to Puerto Rico's state Medicaid program.

8.4 Uniform Remuneration and Classification Plan

Uniform Remuneration and Classification Plan (~\$50 million – Recurring): The plan is intended to establish scales that reflect and guarantee the principle of equal pay for equal work and serves as a basis for evaluating employee performance, ultimately optimizing the administration of Government career employee functions, and improving the quality of life of career public service employees. The intention of the investment is to commence implementation of civil service reform in key agencies, including Treasury Department, Department of Family and related entities, Human Resources Management & Transformation, Office of Management and Budget, and Office of the Financial Institutions Commissioner. Beginning in FY23, these initiatives are assumed to grow by Puerto Rico Inflation.

⁴³ The working capital facility is considered a use of the Commonwealth balance sheet, not a fiscal plan expense.

8.5 Parametric insurance

Parametric Insurance (~\$82 – Recurring): Following steps already taken by some mainland jurisdictions, such as Louisiana and Utah, and considering the aftermath of the 2017 natural disasters, the Government plans to acquire a Parametric Insurance Program, which is a proven and viable alternative to traditional Property Insurance Policies, for said types of natural disasters, including earthquakes. The proposed Program, which is outside the proposed FY2022 budget, would cover both Central Government Agencies and key Component Units (CU) (in terms of services offered). Unlike traditional insurance policies, parametric insurance policies are not subject to legal interpretation (there is no claims adjusting process involved). These programs do not indemnify the pure loss, but rather provides an *ex-ante* payment upon occurrence and certification of pre-determined and pre specified natural events, subject to a series of pre-defined triggers. The benefits of parametric insurance are three-fold:

- **Liquidity:** In the event of the occurrence of a predetermined and specified event, the Government would not be left cash-strapped since there is no adjusting process involved, provided the predetermined event triggers are met. Hence, liquidity would be readily available to the Government, much faster than with a traditional Property Insurance Policy; this liquidity will allow the Government to restore services in a more expedient manner
- **FEMA Recovery Policy Compliance:** According to the Stafford Act, Pub. Law 100-707 (1988), as amended, “(w)hen FEMA provides an applicant assistance for permanent work...the applicant must insure that facility against future loss...”. The annual cost of this Program is estimated at \$82 million, while the Limit of Liability would be \$1.5 billion and will reduce the current “uninsured gap” from \$2.3 billion to \$800 million. Pursuant to applicable federal regulations, this \$800 gap could be justified as acceptable after certification by the Office of the Insurance Commissioner, and acceptance by FEMA, that this approach is a commercially reasonable alternative to protect against future losses. On March 19, 2019, FEMA issued a letter to the Government stating that they are evaluating if the Parametric Insurance approach is an acceptable approach to cover the current “uninsured gap”.
- **Gradual reduction of insurance costs:** Currently, the Government and key Component Units, spend around \$150 million in annual premiums for traditional Property & Casualty Insurance Programs (excluding Municipalities); the Government intends to gradually reduce this spending during the next 3-4 fiscal years, once the Parametric Program is in place and said program matures moving forward.

Beginning in FY23, these initiatives are assumed to grow by Puerto Rico Inflation.

8.6 Other Investments⁴⁴

- **Other Incremental Recurring Investments (~\$105 million):** The 2021 Fiscal Plan includes incremental initiatives the Administration believes will further improve society. Beginning in FY23, these initiatives are assumed to grow by Puerto Rico Inflation.
- **Other Incremental Non-Recurring Investments (~\$61 million):** The 2021 Fiscal Plan further includes one-time FY2022 incremental investments for the Department of Health, PRITS, Public Broadcasting Corporation, Debt Audit, Natural and Environmental Resources, and Central American and Caribbean Games. These initiatives are assumed to be one-time in FY2022.

⁴⁴ Excludes initiatives assumed to be funded by unallocated general fund capital expenditures in the FY2022 budget submission.

8.7 Growing the manufacturing sector in Puerto Rico

The Government has striven for and continues to make Puerto Rico an attractive location for onshoring manufacturing, a key contributor to Commonwealth revenues. Several of the world's largest pharmaceutical and medical device companies already have manufacturing operations on the Island and the onset of the pandemic only furthers the importance of onshoring manufacturing⁴⁵.

The Government has prioritized collaboration with the Federal Government. President Biden announced the plan to sign an executive order strengthening the existing “Buy American” provision to support US manufactures, businesses, and workers, which directly names Puerto Rico as a participant in the partnership.

Additionally, in August 2020, Jennifer González (Resident Commissioner of Puerto Rico) and Marco Rubio (US Senator from Florida) began to advance the Medical Manufacturing, Economic Development, and Sustainability Act of 2020 "(MMEDS Act), which aims to secure national medical supply chains and develop economically “distressed zones”. This would enable Puerto Rico to position itself as a “hub” or national production center of medical equipment and drugs. However, the bill has not yet been enacted into law, but two global bioscience corporations (CytoImmune Therapeutics and Biosimilar Sciences US) have recently announced to move their headquarters and manufacturing operations to Puerto Rico.

⁴⁵ “Bioscience Industry in Puerto Rico” – Invest PR 2020.

PART V: Restoring growth to the Island

A sustainable fiscal and economic turnaround depends largely on comprehensive structural reforms to the economy of Puerto Rico. Only such reforms can drive growth in the economy, reversing the negative growth trend over the last decade or so and enabling the Island to become a vibrant and productive economy going forward. To reverse the negative economic trends, the Government will pursue the reforms outlined below. The impact and timing of these reforms has been adjusted to reflect delays caused by various forces, but the Government continues to believe in these reforms due to their potential economic impact.

The Government's prior fiscal plan submissions focused on fiscal and economic reforms to address the aftermath of discrete, single-event crisis (such as hurricanes and earthquakes). The COVID-19 crisis poses a new challenge that is ongoing and much more profound. Even though the Government has kept the existing reforms, it has adjusted the timing for the completion of some of the reforms. It is uncertain whether the timing of the implementation of these structural reforms can be maintained.

Chapter 9. Structural Reforms

9.1 Human capital and welfare reforms

These reforms will improve workforce participation and the well-being and self-sufficiency of welfare recipients, resulting in a cumulative GNP impact of 0.15% by FY2026. The impact is enhanced in the long-term as **K-12 education reforms** begin adding an additional 0.01% GNP impact per year starting FY2037 resulting a cumulative impact of 0.10% by FY2046.

- **Earned Income Tax Credit (EITC)⁴⁶:** The EITC is a benefit for working people with low to moderate income. The EITC reduces the amount of taxes owed and may result in a cash refund if the benefit is higher than owed taxes. The credit is an effective anti-poverty tool, empowering beneficiaries to defray the cost of education, training, and childcare and support their own self-sufficiency. From 2006 to 2014, Puerto Rico had a Worker's Tax Credit, which was later discontinued due to its ineffective application. This prior Worker's Tax Credit applied to 45% of all tax filers at a cost of \$152 million in its last year of implementation. It was smaller than federal EITC programs (\$150 to \$450 versus ~\$2,000 average credit) and did not eliminate high implicit tax rates on low-income employees or do enough to incentivize formal employment⁴⁷. The EITC program would cost approximately \$205 million per year, but the program will raise formal labor force participation significantly, providing a positive return on the investment. The Government has been successful in implementing the EITC which will continue to be included in the 2020 Tax Year Filings and beyond. The 2020 Certified Fiscal Plan stated the Government did a poor job at promoting the EITC. This is in contrast to what was stated in the Certified Fiscal Plan, which also said the Government had a robust promotional campaign that included publications in Newspapers, Online Campaigns, TV, Social Media and Radio. The EITC is also included in all convention and presentations given by Hacienda spokespeople. In addition, the 2020 Certified Fiscal Plan suggested that ADSEF handle all Promotional Efforts for the EITC for the 2020 tax year filings. Following this, the Government has aligned itself with the Oversight Board and has

⁴⁶ Legislation pending approval in Congress.

⁴⁷ New York Federal Reserve Bank, 2014.

transferred all future responsibility of the Promotional Efforts to ADSEF since ADSEF has direct contact with the majority of the population that will apply for the EITC.

- **Child Tax Credit (CTC)⁴⁸:** As part of the 2021 Fiscal Plan the Government proposed an additional Reform to the Human Capital and Welfare reform. The Child Tax Credit is similar to the EITC Credit awarded during the tax filing season. This credit is for individuals who claim a child as a dependent and provides a credit of up to \$2,000 per child under age 17. If the credit exceeds the taxes bill, families may receive up to \$1,400 per child as a refund. The child will have to meet additional criteria other than age to be considered as a dependent for the CTC. Puerto Rico currently has a CTC but only for families with three or more children who qualify as dependents. The goal of the Government is to make Puerto Rico's CTC equal to that of the mainland U.S. jurisdictions which would include families that have any number of children. This inclusion would help 355,000 families qualify for the CTC which could result in an estimated \$300 million in credits that can be injected into the local economy. A proposal is currently being reviewed in the House of Representatives.
- **NAP Work Requirements:** NAP, Puerto Rico's largest welfare program, is like the mainland Supplemental Nutrition Assistance Program (SNAP) but is funded and administered separately and does not include a work requirement nor specific budget allocations to administer such requirements. To further support labor force participation, the 2020 Certified Fiscal Plan required that the Government introduce a work/volunteer requirement for select adult NAP beneficiaries by FY2022. As part of the human capital and welfare reform package, the Government will institute work requirements with a 4-year phase-in period beginning July 1, 2022 for able-bodied adults without dependents in order to qualify for NAP benefits. Like mainland SNAP, this work requirement must become effective after the individual has collected NAP benefits for three months. The work requirement may be satisfied with 80 hours per month of paid work, volunteer work, and/or qualified training and education. General exceptions would include those under age 18 or over age 60, parents with dependents under age 18, as well as those who are medically certified as physically or mentally unfit for employment. Children, even if their parents do not work, will continue to receive the benefit. The phase-in is the most viable approach given high unemployment rate (lack of supply of jobs), and high volume for training and re-training (lack of skilled professionals) has become a stumbling block that could endanger the current benefits provided by the NAP Program. The Phase-In period had to be delayed due to the impact of COVID-19 on the island particularly those receiving NAP Benefits. ADSEF had to shift its focus during the year to assist COVID-19 efforts throughout the island. The current Government's implementation timeline will be aligned with the Oversight Board's expected timeframe in the next year.
- **Workforce Innovation and Opportunity Act (WIOA):** The Government has already updated the WIOA State Plan to focus its programs and incentives on high-priority sectors and capabilities (e.g., aerospace, software development, and creative services) including COVID-19 related industries that can be beneficial to the Island. WIOA is the primary way in which the Federal Government invests in adult education and workforce development, and it is designed to help jobseekers access employment, education, and support services to succeed in the labor market, and to match employers with the skilled workers they need. The Government will broaden the list of core industries that qualify under WIOA and focus on high impact economic sectors to provide a skilled workforce that meets the needs of employers in each specific region. It will integrate this WIOA program with the broader promotional efforts of the Department of Economic Development and Commerce (DDEC) as

⁴⁸ Legislation pending approval in Congress.

stated in the 2020 Certified Fiscal Plan. In addition, the 2020 Certified Fiscal Plan requested the Government promote the execution of Memorandum of Understanding (“MOU”) between local worker training boards and Government agencies to strengthen training and development while reducing costs. Although progress in this reform has been slow and the impact of COVID-19 has further delayed the execution of MOU’s and the provision of training, the Government has been able to continue offering some workforce programs. Going forward, the Government will focus on key enablers such as creating strong development programs, continue their analysis of the current labor market to adequately update the WIOA State Plan, reduce the current barriers of employment, and begin preparing and helping high schoolers and college graduates obtain skills that will in turn help them find jobs in the Island’s high priority sectors.

- **New Investments in Workforce Development:** The Government has decided to include a budget of \$30.5 million (recurring) for new investment to increase the development of workforce participation for Recent Graduates & Retirees, and increase hiring of Social Workers, Family Services Technicians, and other Child Protective Services. \$15 million (recurring) is directed towards a pilot program to promote first employment opportunities among recent college graduates as part of a larger initiative to address the departure of young professional from the Island thus increasing the Island’s formal workforce. \$9 million (recurring) will go towards the development of a program that will provide part-time employment to retirees, increasing the retiree’s income without directly affecting their retirement benefits. \$6.5 million (recurring) will be used to hire Social Workers, Family Services Technicians, and other Child Protective Services in technical and professional divisions that are currently understaffed.

9.2 Ease of doing business reforms

These reforms will improve conditions for economic activity, job creation, and business vitality, resulting in a cumulative GNP impact of 0.30% by FY2025.

- **Improve Ease of Doing Business World Ranking:** One of the best ways to increase economic growth is to attract additional investment and create new jobs. In 2020, *Doing Business*—an independent assessment of the ease of doing business in 190 economies—rated Puerto Rico the 65th most business-friendly economy in comparison to mainland U.S.’s #6. It is important the Island improves its score to at least the level of Mexico (49th) the highest ranked country in the Caribbean & Latin America. The Island must improve its business-friendliness and consider ease of doing business reforms to support economic growth. The competitive environment in Puerto Rico requires improvement if it is to compete with other investment destinations, specifically by reducing a variety of inefficiencies related to building, expanding, and attracting businesses. Easier-to-navigate regulations, less complex and faster investment and permitting mechanisms, and streamlined tax administration systems can encourage new businesses to hire employees and invest in growth. These outcomes can be achieved by making necessary administrative and legislative changes and by investing in digitization.

The Doing Business Report for 2021 that was set to be published on August 27, 2020 has been delayed following a report that various irregularities in changes to data were found in previous reports. It is expected to be published in the coming months with corrections to the irregularities. Puerto Rico will achieve a best-in-class business environment by taking targeted steps to improve rankings in key identified Doing Business Index indicators by FY2023, with the goal of closing the gap with the mainland U.S.:

- **Overall:** Move from 65 in 2020 to at least 57⁴⁹
- **Construction Permits:** Move from 143 in 2020 to at least 87
- **Registering Property:** Move from 161 in 2020 to at least 95
- **Paying Taxes:** Move from 163 in 2020 to at least 99
- **Getting Electricity:** Move from 92 in 2020 to at least 59

The 2021 Fiscal Plan re-iterates the need for urgent action, particularly in light of the COVID-19 pandemic. As economic activity slows down, companies look to shift supply chains back to the US, and other economies implement rapid reforms to capture growth, instituting ease of doing business reforms is critical. In the aftermath of the pandemic, many firms—especially small businesses—will continue to face significant headwinds (e.g., falling demand for their goods and services), underscoring the need to generate economic activity and attract new investments across the Island. And, while delaying reforms will undermine Puerto Rico’s ability to recover from the pandemic, failure to institute them will enable mainland states and rapidly reforming countries to out-compete Puerto Rico for key investments, such as pharmaceutical manufacturing facilities.

- **Permitting Reform:** The 2020 Certified Fiscal Plan required that the Government implement operational changes to the permitting process, overhaul the Single Business Portal (“SBP”) and Launch Red Tape Commission to help identify operational and technical reforms to the permitting system.

The Government has acknowledged action items set forth in the 2020 Certified Fiscal Plan and has begun their implementation. Nevertheless, struggles have arisen through the process including COVID-19, and funding and personnel issues have made the implementation of these changes more difficult than expected. To mitigate some of these issues, OGP and the UPR have begun creating a Task Force to train UPR students in areas where the Permitting Process is lagging the most (e.g., inspections, permit processing). The New Administration has already adopted a plan to improve the permitting process which includes the automatization of the process through the SBP, includes a self-certification process which is later to be subject to checks and inspection. In addition, the development of an Online Access Electronic Identity System is being considered to give Government agencies electronic access to files that are already in possession of the government, thus eliminating the need for citizens or corporations requesting a permit to re-submit documents or information to individual agencies.

- **Reduce occupational licensing:** Reducing occupational licensing requirements can encourage activity in the formal labor market. The current occupational licensing requirements hinder the possibility of certain workers entering the formal workforce by creating lengthy wait times for license approval. Per 2020 Certified Fiscal Plan it must also consider harmonizing Puerto Rico’s occupational licenses to those in the mainland U.S., especially for states such as NY, FL, NJ, and PA which have a high population of Puerto Ricans. Reciprocity with states enables professionals with licenses from other states to enter the Puerto Rican labor market without undue barriers. The Government has created a Task Force which includes members from the Dept. of State, the Health Dept., and the Puerto Rico Tourism Company. The task force has taken inventory of all occupational licensing requirements and has begun developing reforms to reduce unnecessary regulations, creating a more open labor market. They have also begun identifying licenses that can be eliminated and are identifying bottle necks in the licensing process.

⁴⁹ In line with the top ranked Latin American country in 2018.

- **Improve ease of paying taxes:** The Government has developed a one-stop tax registration and payment portal. During the 2019 tax season, all filings were available to be submitted through the SURI Platform. The 2020 Certified Fiscal Plan stated other tax payments such as Property and Municipal taxes be integrated into the SURI Platform to fulfill the objectives of reducing the time to process tax filing and the time to complete audits. The Oversight Board acknowledges the improvements to the SURI Platform but reiterated the need to reduce the time of post-filing audits.
- **Invest Puerto Rico (IPR):** IPR was created with the purpose of attracting offshore investment (especially from the U.S.). Attracting job-creating investments is crucial to Puerto Rico especially after the recent natural disasters and now COVID-19. IPR will play a crucial role in supporting economic growth and creating jobs necessary to help Puerto Ricans economically recover. Stronger investment promotion will help ensure that the Island can effectively compete with mainland jurisdictions and other countries for critical investments aligned to the Island's competitive advantages. Unlike other Investment Promotion Agencies in the U.S., IPR has been expected to deliver high number of leads & investments while being underfunded. The 2020 Certified Fiscal Plan required the Government to increase funding for IPR promotional efforts, as an example, Vivienda allocated \$7 million in CDBG-DR funds to IPR. Despite lack its of funding and the pandemic, IPR has been able generate over 3,000 leads and 1,500 prospective opportunities which have resulted in 3,500 committed jobs with an average payroll of \$51K, and \$58 million in committed in Capital Investment. Further, IPR has published quarterly reports to monitor progress and address growth opportunities on the Island.

It is also important to note the new administration requires increased collaboration between IPR, DPR and DDEC in order to increase Puerto Rico's economic advantages and attractiveness.

- **Discover Puerto Rico (DPR):** To continue Puerto Rico's transformation into a leading tourism destination, the Government must increase resources for DPR, the Island's Destination Marketing Organization (DMO). DPR has a smaller mandate and lower budget in comparison to other DMOs. The typical DMO markets to six distinct segments: visiting individuals and families; groups; Meetings, Incentives, Conferences, and Exhibitions (MICE); events; residents; and airlines. DPR, is only responsible for marketing to individuals, groups, and MICE; PRTC continues to manage event, internal, and airline marketing. DPR also has a smaller budget than other Caribbean destinations—\$25 million (or \$943 per available hotel room) compared to an average budget of \$40.8 million (or \$1,485 per room) for Caribbean DMOs. Even with these constraints, DPR had shown success in increasing tourism to the Island pre-COVID. It is important DPR adjusts their Promotional Plans to increase tourism and promote Puerto Rico as a COVID-19 responsible tourist destination. DPR must collaborate with IPR and DDEC to increase attraction to the island, educated small businesses affected by the pandemic about all available government assistance, and to develop a strategic plan for the 500-year anniversary celebration of the founding of San Juan.

9.3 Power sector reforms

An affordable, reliable, safe, and resilient electric power service is essential for the island's sustained economic growth and development. Electricity is a fundamental enabler of the people of Puerto Rico's livelihoods, and remains a critical service that needs to be safeguarded, particularly considering the outsized catastrophic events in 2020 (e.g., January 2020 earthquakes, COVID-19 pandemic). And as an important element of household and business activity, electricity is also a critical factor for attracting and maintaining investment in Puerto

Rico. The Puerto Rico Electric Power Authority (PREPA) has been responsible for providing electricity to Puerto Rico since 1941 and is a public corporation owned and operated by the Government.

However, PREPA has been encumbered by numerous financial and operational issues. Over the years, PREPA was unable to update rates to cover base operating costs, invest in modernizing the energy system, or fully fund the pension system. Furthermore, PREPA incurred significant legacy debt obligations, and was unable to implement a long-term capital improvement program.

This operating model created an untenable financial situation for PREPA. Politicized management and volatile fuel prices exacerbated by declining demand and an economic contraction, resulted in PREPA's inability to service its debt, and ultimately resulted in PREPA seeking PROMESA Title III bankruptcy protection in July 2017⁵⁰. For more than a year prior to filing for bankruptcy, PREPA lacked access to the capital markets to help fund grid and generation modernization investments, further contributing to the poor quality of service experienced by the island's residents and businesses resulting from the deteriorating infrastructure.

Underinvestment and underdevelopment of the grid, poor maintenance practices, and workforce losses all contributed to a chronically poor performing power sector. Puerto Rico has twice as many forced outages as the US industry average⁵¹. PREPA also significantly underperforms against mainland utilities on multiple operational, reliability, and customer service metrics.

Over the next five years, the power sector in Puerto Rico will continue its transformation and modernization to support the delivery of reliable and affordable power. As mandated by Act 17-2019, known as the Puerto Rico Energy Public Policy Act, the government should continue to implement its comprehensive energy sector public policy reform to enable a successful transformation and modernization that supports the delivery of reliable and affordable power unlocking the resulting growth from the Fiscal Plan projects. The successful transformation of Puerto Rico's power sector principally depends on:

- **Implementing regulatory reform:** A strong and independent energy sector regulator, as set forth under Act 17-2019, is essential to provide certainty and stability in the energy market, promote much needed investments, and enforce compliance with the energy sector transformation's objectives. In recent years, the framework of regulatory reform has been approved and an independent regulator (i.e., PREB) has been established. The focus in coming years will be to continue supporting the independence of the regulator and enabling the regulator to execute on its mandate. This will be accomplished by developing and strengthening the regulatory framework and promoting greater transparency and accountability.
- **Transitioning the operation and management of PREPA's electricity grid and generation assets to private operators:** Transitioning to a private operator to manage, operate and maintain Puerto Rico's Transmission and Distribution (T&D) network is key to improving and maintaining operational performance and customer service, support rigorous capital project execution to modernize the system, strengthen grid resilience, and ensuring ongoing fiscal balance and control. In early 2019, Puerto Rico's Public-Private Partnership Authority (P3A), began a process to evaluate and select a private operator to assume responsibility for managing and operating the T&D system. This procurement process culminated during the summer of 2020 with the selection of LUMA Energy and the execution

50 "Puerto Rico's Power Authority Effectively Files for Bankruptcy", New York Times, 2 July 2017.

51 "A review of PREPA's generation patterns reveals that PREPA, in fact, increased its reliance on the diesel generation fleet in FY2015 and FY2016, doubling its use of distributed generation turbines and tripling its use of the diesel Aguirre CC plant." Fisher and Horowitz, revised November 23, 2016, Expert Report, 21.

of an O&M Agreement between the P3A, PREPA and LUMA Energy. PREPA, P3A and LUMA Energy are currently working on the front-end transition process required under the T&D O&M Agreement for the system's operational transfer from PREPA to LUMA Energy scheduled for June 2021.

- A similar process is currently underway by the P3A to select potential private operator(s) for PREPA's generation assets. After issuing an RFQ and receiving statement of qualifications from fifteen (15) proponents, P3A shortlisted eight (8) world class proponents which are currently participating in the RFP process. P3A expects to select private operator(s) for PREPA legacy generation assets during the fourth quarter of calendar 2021.
- **Restructuring legacy debt obligations:** In order to fund the transformation of Puerto Rico's power sector, PREPA will require access to capital markets. Given the utility's significant legacy debt obligations, a sustainable restructuring plan is necessary for PREPA to exit bankruptcy and regain access to credit. Under a restructuring transaction, customers will experience lower rates than those that would otherwise be necessary to pay PREPA's legacy debt. Ultimately, a successful restructuring of outstanding bonds and debt obligations will allow PREPA to achieve its transformation goals, thus modernizing Puerto Rico's power grid, and passing on subsequent efficiencies and cost savings to customers.
- PREPA's Fiscal Plans and the Government's energy sector laws and regulations⁵² lay out the transformation road map. If successfully implemented, a reformed energy system will lead to a modernized and reliable energy service across the islands: a diversified fuel mix and reduced fuel costs, anchored on modernized and efficient generating resources which reduce price volatility; increased operational efficiencies and environmental compliance; and a well-funded, financially sustainable utility. These outcomes will benefit the customers and businesses of Puerto Rico in enabling a more affordable, reliable, and safe electricity service.

9.3.1 Energy regulatory reform and oversight

The current regulator of the power sector in Puerto Rico is the Puerto Rico Energy Bureau (PREB), which has been operational since its creation by Act 57-2014, as amended. PREB has the responsibility to "regulate, monitor, and enforce the energy public policy of the Commonwealth of Puerto Rico."

As Puerto Rico's energy sector continues its transformation into a vibrant, modern system, PREB will continue to be responsible for the development of a robust regulatory framework that will promote prudent investments by utilities, increase quality of service to customers, and ensure industry trends and technological advancements are appropriately incorporated into Puerto Rico's energy system. To that end, PREB's regulatory oversight will directly impact the utility and have significant influence on Puerto Rico's energy sector. To fully achieve its purpose, PREB should remain financially independent from the Government and its decisions, and its determinations should be free from any political influence or interference.

9.3.2 Long-term mandate, authorities, and expertise for the energy sector regulator

To be effective, PREB's regulatory authority and its mandate to promote an efficient, reliable, resilient, and customer-responsive energy system must be clear and well-established. PREB's legislative responsibilities can be categorized as (1) rate setting, (2) Integrated Resource Plan (IRP) approval and compliance, and (3) protecting customers.

⁵² Puerto Rico Energy System Transformation, Act No. 120-2018; Puerto Rico Energy Policy Act, Act No. 17-2019.

- **Rate setting:** PREB should “review and approve and, if applicable, modify the rates or fees charged by electric power service companies in Puerto Rico.”⁵³ In doing so, PREB should ensure rates and rate structure are rational and predictable, minimize risk and “rate shock”, and create incentives to support equitability and economic development. PREB should set a clear, transparent, and efficient process for rate cases. All rate adjustments and revisions must be approved by PREB before enactment. In this capacity, PREB must ensure that necessary operational frameworks are in place to not only provide a robust review process in line with best-in-class mainland US state regulators (e.g., New York), but also ensure that rate reviews are conducted efficiently and in a manner that does not adversely impact service performance or consumer confidence.

In future rate cases, PREB should encourage several core principles to be incorporated including dynamic rate structures (e.g., time of use, rate decoupling, unbundling), prudence of investments, cost of service, and distribution of cost and revenue allocation.

- **Integrated Resource Plan (IRP) approval and compliance:** PREB is mandated to “review and approve policies and strategic plans...in connection with energy resources integrated planning in Puerto Rico, and oversee compliance therewith.”⁵⁴ During review, PREB should assess related policies and plans on whether they meet the objectives of Puerto Rico’s energy public policy and promote energy service reliability, safety, efficiency, and affordability. During implementation of the plan, PREB should fulfill its role of ensuring there are no impediments to the integration of renewable resources, establishment of demand response or management and adoption of energy efficiency programs.
- **Protecting customers and customer service:** PREB should be responsible for ensuring customers are reasonably protected in the energy system for factors such as affordability, information accessibility, and quality of service. This includes reviewing potential policies, rates, and capital projects for their potential effects on customers, and ensuring impacted customers understand and have the ability to respond in due course. Ultimately, PREB and the *Oficina Independiente de Protección al Consumidor (OIPC)*⁵⁵, as part of the Regulatory Board of Public Services, hold the responsibility of evaluating and providing determination in all cases of consumer complaints regarding pricing and quality of services provided by PREPA.

9.3.3 Expertise

To implement its long-term mandate in a robust and effective manner, PREB should continue to build expertise on topics that reflect the core regulatory priorities facing most regulators:

- Generation planning and dispatch
- T&D reliable operations and capital planning
- Workplace safety
- Customer service
- Rate-making

In addition, PREB can develop further expertise in topics that are increasingly addressed by regulators across the mainland so that Puerto Rico’s energy sector is able to match pace with

53 “ABOUT THE PUERTO RICO ENERGY BUREAU” <https://energia.pr.gov/en/about-the-commission/>.

54 “ABOUT THE PUERTO RICO ENERGY BUREAU” <https://energia.pr.gov/en/about-the-commission/>.

55 Independent Office for Consumer Protection (IOPC).

best-in-class utilities. By doing so, PREB can provide proper guidance to sector players on how to secure, modernize, and efficiently operate the grid. These topics include:

- Contribution-in-lieu of taxes (CILT)
- Renewable energy integration (distributed and commercial)
- Weather-related risks (e.g., hurricanes, climate change)

9.3.4 Structural elements to ensure a best-in-class regulatory agency

Although administratively located within the Puerto Rico Public Service Regulatory Board (PSRB), PREB's decision-making process should not be subject to direct or indirect review by other government entities, except for any review under applicable administrative procedure rules. Staff involved in substantive decision-making should be kept separate and independent from the PSRB and be fully dedicated to matters within PREB's jurisdiction and purview. PREB may, on an annual basis, provide funds to the PSRB to cover administrative and other operational costs, however, PREB's resources should be kept separate and shall not be controlled or placed under the direction of the PSRB.

There are five key structural elements that will ensure PREB is a best-in-class regulatory agency:

- **Governance:** It is imperative that PREB's governance structure enable quick and robust decision-making. In line with best practices for regulatory commissions (e.g., California Public Utilities Commission, Hawaii Public Utilities Commission, New York Public Services Commission), PREB is headed by five commissioners who serve staggered six-year terms. The commissioners are appointed based on their technical, professional and/or academic credentials. The commissioners should be supported in their oversight role by professional civil servant staff that has utility expertise.
- **Independent customer advocate:** All commission decisions in adjudicatory proceedings must comply with applicable requirements of administrative procedure. Separate from the regulator, there shall be an independent customer advocate, a role currently filled by the *Oficina Independiente de Protección al Consumidor* (OIPC). OIPC should be well-funded so that it has the resources to meet its responsibilities. Currently, PREB transfers 10% of its budget to OIPC; as priorities evolve and the need for a robust consumer advocate increases, the government may provide OIPC with additional funding.
- **Employee structure:** Presently, PREB must develop and implement a plan for transitioning from its existing employee structure to a structure comprised of no less than 75% civil servant employees and no more than 25% trust employees⁵⁶. In the future, PREB must minimize the percentage of trust employees to 15%, and ultimately 10%. During and after the energy sector reform process, PREB must have enough staff to effectively undertake its duties and responsibilities in a timely and professional manner.
- **Budget:** PREB's substantive independence must be supported by financial independence. Under current law, PREB's yearly budget is set at \$20 million and collected through charges assessed on certified energy companies⁵⁷. To provide for a steady and predictable funding source, PREB's enabling act must be amended to provide that PREB's budget shall be funded entirely through rates, as part of the revenue requirement used to determine energy rates. PREB's funds are then collected by the T&D operator through customer bills and periodically remitted to PREB. This funding mechanism is consistent with the mechanisms used to fund

⁵⁶ "Trust employees" includes any employees that are related to political appointments, non-civil service appointments, etc.

⁵⁷ Amount in line with other jurisdictions; the Hawaii Public Utilities Commission had revenues of \$19M in FY2017 to serve a population of 1.4 million.

peer mainland regulators. Providing for an independent and unencumbered source of income for PREB helps create the conditions to protect ratepayer interests, increase transparency and reduce system costs. PREB's budget and funding must be kept separate and independent from the Commonwealth budget or the budget of any other Commonwealth agency, entity, or instrumentality, and neither the Executive nor the Legislative branches shall have authority to modify PREB's budget or reappropriation any of PREB's funds without PREB's prior consent. However, PREB is subject to periodic reviews from relevant authorities for use of public funds, which is consistent with all other government agencies in Puerto Rico.

- **Transparency:** To achieve best-in-class status as an energy system, transparency is an indispensable factor. PREB must ensure that proactive transparency permeates relevant energy operations (i.e., this should exclude confidential information such as customer data and operational details that would increase cyber or risk vulnerabilities, etc.). This may include making information publicly accessible, maintaining quick and efficient decision-making, and holding public events when appropriate in order to consider public opinion. Additionally, PREB must uphold transparency in its own financials and operations, including disclosing how it utilizes its annual budget.

9.3.5 Vision and structure for an energy system operator

Private operators for T&D and generation operations will be responsible for executing Puerto Rico's energy system modernization strategy as well as assisting with the allocation of related federal funding. Each private operator's overall objective must be to improve service quality and deliver reliable service at just and reasonable prices. As such, a private operator must be incentivized and motivated to deliver financial and operational performance improvements across five dimensions:

- **Reduced costs by introducing experienced personnel.** A private operator would be incentivized to reduce PREPA's dependency on outsourced contracts by insourcing activities, empowering the local labor force, and potentially achieving economies of scale.
- **Upgraded technology.** While PREPA has limited access and experience with industry-standard technology, a private operator must be incentivized to deploy modern grid technologies, digital capabilities, and infrastructure to significantly enhance operational efficiency, thus lowering O&M costs and customer rates over time through better asset utilization.
- **Improved processes and procedures.** Drawing on operational expertise, a private operator should be incentivized to streamline and standardize critical management processes and implement operational efficiencies (e.g., processes such as procurement, contract management, maintenance, etc.). A private operator can also leverage experience in customer service to improve PREPA's responsiveness to customer needs and expectations.
- **Limited political interference.** A private operator's decisions must be subject to independent regulatory oversight, but free of political interference. This would lead to the adoption of standard industry practice where experienced utility operators make operational decisions with oversight from an independent regulator (e.g., investment decisions made based on overall benefit to the system, instead of short-term political gains).
- **Effective and efficient capital delivery.** A private operator should also be incentivized to establish the tools and processes critical to improving PREPA's capital project management. This will be key to optimizing the use of the federal funding required for grid modernization improvements, which in turn will aid PREPA in strengthening grid resilience.

9.3.6 Energy sector debt restructuring

As of May 2017, PREPA had \$9.25 billion of outstanding bond and other debt obligations, and an unsustainable repayment schedule; PREPA would have had to repay approximately \$4.5 billion of debt service obligations between FY2019 and FY2023. PREPA's unsustainable capital structure reflects persistent operating deficits, resulting from overly low base rates and declining electricity sales since 2006.

To restructure PREPA's debt, a debt restructuring agreement among a group of PREPA creditors, the Oversight Board, the Government, and PREPA is in progress. However, as a result of the uncertain and unpredictable effects of COVID-19 on PREPA and its customers, the Oversight Board and the Government have requested delays in the court process to assess and understand the implications of COVID-19 on the bankruptcy process.

9.4 Infrastructure reform

These reforms, along with capital investment, will improve the flow of goods, services, information, and people across the Island. It has not been scored to provide a specific GNP uptick but will likely contribute a consequential uptick in the Island's long-term development.

■ **Infrastructure and Reconstruction Efforts:** The Government created COR3 to lead the coordination, development and execution of long-term recovery and reconstruction efforts, and facilitate federal funding and private capital to promote a more rapid economic turnaround. The Public Private Partnerships (P3) Authority could serve as counterparty, introducing exclusivity provisions to lower the risk for private capital, and subordinating government-provided capital. The P3 Authority would further seek to leverage the skills and assets of the public and private sectors to service the people of Puerto Rico in delivering prioritized projects efficiently and effectively. Puerto Rico's proven P3 framework and record in executing landmark projects such as Toll Roads PR-22 / PR-5 and LMM International airport highlight the potential for an Island-wide team to develop and deliver technical, financial, and legal expertise for P3 projects. Further investing in these entities can enable their ability to facilitate needed improvements in infrastructure, knowledge services, and other strategically important sectors to improve the fiscal situation in Puerto Rico and spark economic growth and environmental compliance. Additional funding that becomes available for the COR3/P3 Authority could also go towards improving governance and execution. Additional investment in infrastructure projects and recovery efforts through the Puerto Rico Infrastructure Authority (PRIFA) will promote further economic growth and reduce the risk of reform implementation. To avoid the potential for wasteful spending, these investments must adhere to the following principles:

- Set clear priorities using cost-benefit analysis to guide investment
- Accelerate the pre-construction process
- Build sustainable funding models and financing strategies focused on full lifecycle costs of any capital investments
- Promote procurement and project delivery best practices to lower costs
- Build infrastructure of tomorrow

9.4.1 Current state of infrastructure and capital investment

Infrastructure investment as a percentage of Gross Domestic Product (GDP) decreased from 3.3% in 2000 to 1.2% in 2018⁵⁸, in part as a result of the fiscal crisis, but the capital investments enabled by federal disaster recovery funding offer a unique opportunity to make transformational investments that support economic development.

There are several critical elements that Puerto Rico will include to capitalize on the transformational opportunity afforded by historic federal capital funding:

- **Build organizational structures and capabilities** in the Government to prioritize and deliver projects faster and at lower cost
- **Prioritize projects with the highest long-term benefit-cost ratios** taking account a variety of monetizable and non-monetizable benefits
- **Systematically leverage private sector capabilities** to improve overall public outcomes

9.4.2 Organizational Structures and Capabilities

When creating a reconstruction plan, it is imperative to build a central capability with the skills and mandate to design an overall recovery portfolio and oversee efficient project delivery. To address this, The Government created COR3 as a Division of the P3 Authority to lead the coordination, development, and execution of long-term recovery and reconstruction efforts. The COR3 has been created based on leading practices used in many jurisdictions, including New Jersey, Louisiana, New York, and New Zealand, to ensure higher accountability, transparency, and coordination of disaster recovery efforts.

COR3 will aggressively pursue next level resiliency activities with federal dollars, to ensure that Puerto Rico's critical assets are sufficiently protected from future hazards.

Specific COR3 activities will include:

- Developing, presenting, and administering recovery action plans
- Financing, executing, and effecting infrastructure projects related to recovery efforts
- Monitoring contracting for compliance and effectiveness purposes
- Implementing and enforce checks and balances for procurement and approval of contracts and payments
- Coordinating and channeling all efforts and activities of the Government related to recovery efforts
- Monitoring capital project delivery, focused on major projects, to ensure on-time, on-budget delivery, highlight risks of cost overrun or delay, and create transparency for overall capital program delivery, including recovery spending led by COR3 or another Government entity with capital delivery expertise

9.4.3 Prioritization and Delivery

The Government will employ infrastructure delivery best practices (e.g., prioritization of projects for economic impact, fast-track permitting, procurement reform). These best practices improve efficiency and transparency and should be applied to all areas of infrastructure expenditure of

⁵⁸ American Society of Civil Engineers 2019 *Infrastructure Report Card*.

the Government including reconstruction, construction and maintenance of government owned assets, and procurement of infrastructure through public corporations and Public-Private Partnerships.

The Government will pursue five sub-strategies:

1. Set Government infrastructure priorities to guide investment

- Set target outcomes to guide prioritization of projects
- Develop clear, systematic cost-benefit analysis and quantitative scoring to prioritize projects based on return on public investment and the ability to implement

2. Accelerate the pre-construction process

- Identify opportunities for local review and permitting, for as many projects as possible, to avoid federal delays
- For projects requiring local review, revisit existing process to reduce hurdles, and ease of meeting them, wherever possible
- Where federal approval is needed, focus on clarifying decision rights and confirming processes with all major stakeholders; harmonizing local processes to match federal processes and seeking waivers where applicable; ensuring transparency and clarity from Federal Government on where projects are in the pipeline; and utilizing Title V of PROMESA

3. Build sustainable funding models and financing strategies

- Leverage external capital, by expanding P3's and access to federal credit (e.g., the Transportation Infrastructure Finance and Innovation Act (TIFIA)) and grant (e.g., Infrastructure for Rebuilding America (INFRA)) programs
- Increase bankability, and eligibility for participation in P3's by deploying monetary and non-monetary incentives (e.g., recyclability of proceeds from asset monetization, including monetization of Government-owned real estate to support the revenue models for P3's)
- Provide support to de-risk greenfield investment (e.g., reduction of early-stage demand risk)

4. Promote procurement and delivery best practices

For projects that receive Government funding, ensure such projects:

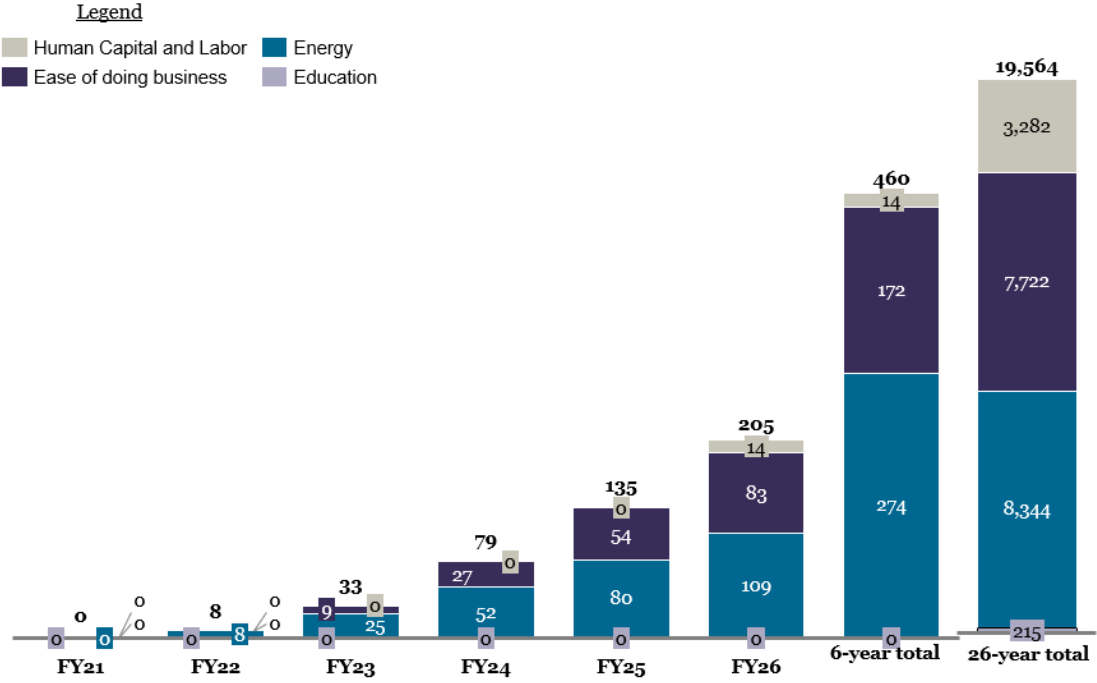
- Develop an aligned owner organization with streamlined processes (e.g., early procurement involvement, accountable owner team oversight)
- Build an effective contracting strategy (e.g., tailored bidding process and pricing models, change order management tools)
- Utilize advanced procurement tools and approaches (e.g., rigorous clean sheet models, quantified view of Total Cost of Ownership drivers)
- Implement lean construction and digital techniques

5. Build the infrastructure of tomorrow

- Identify innovative technologies (e.g., automotive transformations, drones, new tunnel creation methods, the Internet of Things) and develop a strategy to actively promote them (e.g., AV pilot test zones), or at least find a way to not stifle their development (e.g., job trainings for displaced workers)
- Critically evaluate major new investments against future trends, to avoid disruption by innovation (e.g., avoid the buildout of excessive parking given increase in shared mobility and growth of autonomous vehicles)

The 2021 Fiscal Plan assumes the growth from these reforms will reach 0.60% through FY2025. These reforms have an approximately \$19.6 billion positive impact to surplus from FY21 through FY2046.

EXHIBIT 32: ESTIMATED IMPACT OF STRUCTURAL REFORMS



PART VI: Transforming Government to Better Serve the People of Puerto Rico

With the newly elected administration installed, the Government will help its key agencies and departments focus on those initiatives that fulfill its stated priorities; these include to improve the quality of life for everyone in Puerto Rico, to promote economic development and equality in sharing such prosperity, while balanced with fiscal responsibility. Prioritization has also been given to those initiatives that will create a more transparent and efficient government, thus fostering government operations that strive for excellence in every way. In building this new fiscal plan, these priorities were applied to initiatives that were already underway and deserved continued attention and effort as well as to new initiatives that have been prioritized for the new year.

As in prior fiscal plans submitted by the Government, the 2021 Fiscal Plan does not go into the granular detail of defining savings by measure/agency but instead provides brief descriptions of these prioritized measures selected to yield the greatest impact for the people of Puerto Rico.

Fiscal measures

The 2021 Fiscal Plan builds on the goals of 2020 by continuing to prioritize changes to promote efficient, high-quality, sustainable Government services for the people of Puerto Rico. The model rests on four pillars focused on Quality of Life for the Commonwealth, Economic Development, Excellence in Government and Fiscal Responsibility, all driving a healthy and thriving Puerto Rico.

Agency Efficiencies: Agency Efficiencies include reform initiatives in the Departments of Education, Health, Public Safety, Corrections, OCFO, and Economic Development, as well as consolidations and reductions within the long tail of other agencies.

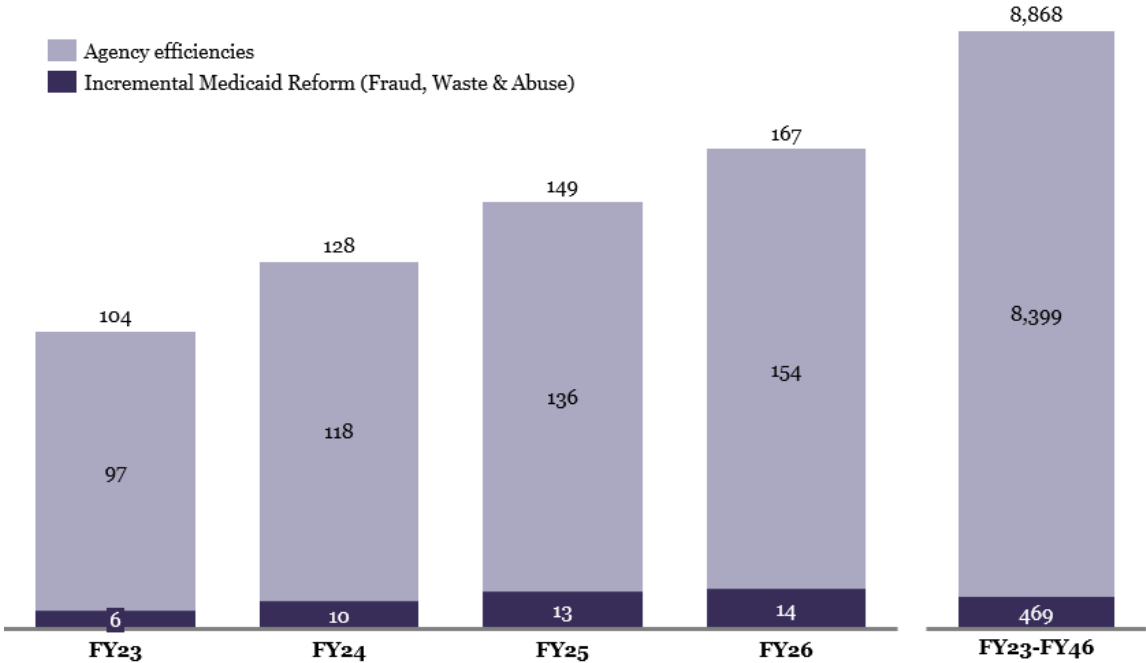
Office of the CFO: The Office of the CFO (“OCFO”) will be responsible for, and crucial, to ensure the most efficient financial stewardship of the Island’s resources.

Medicaid Investments and Reform: Healthcare measures seek to reduce the rate of healthcare cost inflation through measures to reduce fraud, waste and abuse, and are projected to grow with healthcare inflation.

Tax Compliance and Fees Enhancement: Tax compliance initiatives involve employing technology and other innovative practices, as well as implementing new taxes, to capture revenue from under-leveraged sources. The 2021 Fiscal Plan assumes that tax compliances and fees enhancement measures are embedded in the FY21 General Fund baseline revenue forecast.

Together, the incremental go-forward measures are crucial to the structural balance of the Commonwealth’s budget and are projected to have an impact of ~\$9 billion from FY2023-2046.

**EXHIBIT 33: INCREMENTAL GO-FORWARD FISCAL MEASURES BEYOND FY2022
(IMPACT FROM FY2023 THROUGH FY2046)**



- (1) The 2021 Fiscal Plan includes no further cuts to UPR or Municipal appropriations beyond those included in the FY2021 budget. As such, there are no incremental measures beyond FY2022 related to UPR or Municipal appropriations.
- (2) The 2021 Fiscal Plan includes no pension reform. As such, there are no incremental measures beyond FY2022 related to Pension Reform.
- (3) The 2021 Fiscal Plan assumes that revenue measures related to improved compliance (PIT, CIT, and SUT), Earned Income Tax Credit, and Right Rate Taxes & Fees are imbedded in the FY2021 baseline forecast and complete at the end of FY2021. As such, there are no incremental revenue measures beyond FY2022.
- (4) The above chart excludes the impact of contra-measures associated with PIT and CIT tax cuts.
- (5) Agency Right-sizing includes Utility Reduction measure

Chapter 10. Agency efficiency reform

To comply with Section 201(b)(1) of PROMESA, a Fiscal Plan must “provide a method to achieve fiscal responsibility and access to the capital markets.” Accordingly, Fiscal Plans are key to the manifestation of Government public policy and of the goals for the people of Puerto Rico to achieve these ends.

Government agencies have executed a number of efficiency measures to drive down personnel and non-personnel operating costs. The focus will now shift to providing Government agencies the tools, **resources**, and insights into leading practices **that** will allow them to reshape their models to focus on efficient, high-quality services, delivered when and where the people of Puerto Rico need them.

As part of the new Government model, the Government is working on consolidating the agency groupings which have completed the legislative process. These consolidations will better focus the competing efforts of multiple agencies, such as the Economic Development grouping, for improved resource utilization. In other cases, the consolidations will serve to better coordinate services for residents, such as the Public Safety grouping. Additionally, consolidations will enable agencies to streamline back-office processes, eliminate duplicative resources and benefit from procurement efficiencies.

In addition to agency consolidations, the Fiscal Plan outlines operational and process improvements that will more efficiently use resources—including staff, equipment, services, and buildings—across agency groupings such as Education (PRDE), Corrections (DCR), Health (DOH), and Public Safety (DPS). The goal of such efficiency measures is to improve the quality of the underlying services for the population while also directing valuable resources toward priorities and achieving the cost savings needed to balance the Government budget.

These measures were developed through an iterative process across the Government and are designed to achieve necessary savings targets without compromising the quality of public service delivery on the Island—and actually improving it in many cases.

10.1 Agency operational efficiencies and improvements

The Fiscal Plan outlines a set of medium-term savings the Government could achieve through both agency-specific and government-wide personnel and non-personnel measures.

10.1.1 *Agency-specific personnel and non-personnel efficiency measures*

There are several actions that have been applied to each agency to achieve these targets:

- **A series of agencies have the potential to be merged** when benchmarking and best practices determine that activities across agencies could be better served through a single mission and management to eliminate redundancies, and/or where economies of scale make shared services more economical without reducing quality of service.
- **A series of agencies will be left independent but made more efficient** through a series of streamlining efforts, allowing the agency to provide improved services at a lower cost to taxpayers.
- **Some agencies will be closed completely or privatized** if their function and programs are not required, or can be transferred to private ownership, resulting in a 100% personnel and non-personnel savings for all non-federal funded expenditures after a two to three-year wind-down period (a minimum of 50% savings must be achieved no later than year two). The

Government proposed six agencies for closure: Model Forest; Culebra Conservation and Development Authority;⁵⁹ Company for the Integral Development of Cantera's Peninsula⁶⁰; Economic Development Bank; Industrial, Tourist, Education, Medical, and Environmental Control Facilities Financing Authority (AFICA); and National Guard Institutional Trust.⁶¹

The Fiscal Plan expects all agencies to follow the guidance and concepts provided in Governor Pierluisi's Approach to an Effective Government (Chapter 7) as they prioritize their efforts towards transparency, responsiveness, efficiency, and execution.

10.1.2 Cross-cutting non-personnel measures

In addition to driving operational improvements specific to service delivery, agencies will reduce spend on utilities as well as on other areas of the budget which have been historically "opaque" in terms of where funds are flowing:

Reducing utility spend over time: The Government will implement energy efficiency initiatives that reduce utility payments in line with mainland energy efficiency efforts such as the U.S. Federal Energy Management Program (FEMP). Energy efficiency initiatives would include facility & fleet optimization (e.g., recycling), improved procurement agreements, and strategic investments, potentially through utility capital expenditure.

Reducing spend on historically low visibility areas: The Government will strive to continuously monitor and reduce expenses in historically low-visibility areas (e.g., "unclassified professional services" and "englobadas").

10.2 Investing to support agency efficiency and recovery

The 2021 Fiscal Plan includes new incremental funding to support the Government in its efforts to operate effectively and sustainably. These include:

- **Immediate funds for COVID-19 response:** The 2021 Fiscal Plan continues to support the distribution of the \$787 million certified as part of the Emergency Measures Support Package and other relief actions, solely focused on mitigating the effect of the COVID-19 pandemic on front line healthcare and public servants, as well as self-employed and small businesses. The package is comprised of \$500 million in additional FY2020 expenditures, a \$157 million reapportionment from the FY2020 General Fund budget, and \$131 million in Restart funds. These funds are intended to provide \$212 million for "hazard pay" for frontline workers (including public and private nurses and technicians, police, certain correctional staff, and professionals managing taxes and financial operations), \$50 million for medical and public safety supplies and capital expenditures, and \$255 million for enabling distance learning in the public education system, \$101 million for municipalities, and \$160 million in one-time direct payments to individuals and small businesses
- **Investments in frontline service delivery:** The 2021 Fiscal Plan includes several incremental investments in frontline service delivery, including compensation and benefit raises for police officers (including backpay for those who are owed overtime payments from past service); support for Special Education therapy, and overdue teacher compensation; funds to attract additional recruits to the Emergency Medical Services Corps and Institute of Forensic Sciences; and investments in healthcare (including funds for opioid treatment,

⁵⁹ Agency will only be partially closed, so funding will be reduced by 32% overall starting in FY2020.

⁶⁰ To be closed on July 1, 2033 per current law.

⁶¹ The National Guard Institutional Trust and Economic Development Bank will close but not achieve any savings.

telehealth, electronic health records, hospital capital expenditures, scholarships for medical students who commit to practice outside of major metro areas, and additional school nurses)

- **Support for accelerating operational improvements:** Given the complexities of the situation, the Fiscal Plan continues to pause new rightsizing measures, which is intended to enable agencies to focus efforts on their roles in the pandemic response and on implementing the necessary operational reforms needed to improve services long-term. Further, the Fiscal Plan will continue to include implementation budget incentives that would become available when certain milestones are accomplished (e.g., consolidation of back-office functions)
- **Funding to enable consent decree compliance:** Several Puerto Rico Government agencies are subject to federal consent decrees that require them to adhere to certain regulations. With these consent decrees often come funding requirements (such as, certain funding levels to Special Education students). The 2021 Fiscal Plan includes funding for the consent decree requirements that the Government is aware of currently

Chapter 11. Office of the Chief Financial Officer (OCFO)

One of the key goals of PROMESA is for fiscal accountability to be quickly and permanently ensconced in the Government. To fulfill this goal, the Government will create a strong Office of the Chief Financial Officer (OCFO). Absent a constitutional amendment or preemptive federal legislation, the creation of an independent OCFO is constrained by existing Puerto Rico constitutional provisions. Specifically, the constitution prohibits the delegation of executive authorities to an independent non-constitutional officer – one not appointed by the Governor and subject to Puerto Rico Senate confirmation. In addition, the constitution provides that the Secretary of Hacienda is third in line for succession to the Governor. Therefore, the optimum solution is to reorganize all the desired OCFO functions within the existing Hacienda constitutional framework, that way the CFO would have the existing constitutional powers, responsibilities and appointment procedures of the Secretary of Hacienda as stipulated in the constitution. By centralizing key financial management functions, the Government will address long-standing issues that have arisen under the Island’s historically decentralized financial management regime. These include persistent difficulties around understanding the financial needs and priorities across Government as a whole based on transparent data, timely and accurate consolidated reporting, preventing the misallocation of funds, preventing agencies from overspending their budgets, control over opening and managing bank accounts and timely consolidated financial statement issuance. The creation of a centralized OCFO was a linchpin in the restoration of fiscal responsibility of several public entities, including the District of Columbia following its financial crisis in the mid-1990’s and the City of Detroit in its Chapter 9 bankruptcy in 2013.

The Government has already made progress in certain areas, including providing bank account transparency, weekly publication of emergency reserve reports, monthly reporting of budget- to-actuals for select Government agencies and publishing of the 2017 tax expenditure report published in September 2019.

Law No. 230 of July 23, 1974, as amended, titled “Puerto Rico Government Accounting Act” was intended to authorize the Secretary of the Treasury to design and audit the fiscal organization, accounting systems, and payment and revenue procedures of the dependencies and entities of Puerto Rico, as well as carry out the central accounting and prepare the financial reports of all government operations.

- In order to fulfill all the above responsibilities, it is necessary for the Government to have a Chief Financial Officer (CFO). The Secretary of the Treasury will be designated as CFO, and will have the following responsibilities: (i) centralize all financial management functions, improving governance and fiscal management; (ii) continue enhancing transparency, strengthening internal processes and controls, and improving the trust among outside stakeholders in the financial management of Puerto Rico; (iii) maintain control and accounting of the public funds and property; (iv) design and audit the accounting and financial units of the agencies, instrumentalities and public corporations that are related to, or involved in the process, control and accounting of the public funds and property; (v) provide the general principles and rules that will be followed in the accounting of revenues, appropriations and disbursement of public funds; (vi) improve the timeliness in publication of the Government's CAFRs and financial reporting provide advice on the preparation and implementation of the tax and revenue public policy of the Government, among other things.

The additional faculties of the CFO include but are not limited to: (i) recommending the Governor of Puerto Rico to appoint receivers to rectify financial matters, pursuant to Act 5-2017, as amended, known as the "Puerto Rico Financial Emergency and Fiscal Responsibility Act"; (ii) coordinating with the Puerto Rico Innovations & Technology Services (PRITS), the General Services Administration and OMB the implementation of a new centralized accounting system (ERP). As part of this responsibility, steps shall be taken to guarantee the integration of centralized procurement modules, pursuant to Act 73-2019, as amended, known as the "General Services Administration Act for the Centralization of Purchases of the Government of Puerto Rico 2019"; (iii) coordinating with GSA the measures required to guarantee promptly paying providers and contractors of the Government; (iv) in coordination with AAFAF, publishing regularly updated reports on liquidity, bank account balances, budget, budget to actuals and other financial information of the agencies of the Government.

The CFO will be supported and advised by the Puerto Rico Fiscal Agency and Financial Advisory Authority (AAFAF) and the Office of Management and Budget (OMB) in their respective areas of expertise. Thus, the CFO will work in coordination with the Executive Director of AAFAF and the Director of the OMB.

In order to fulfill these functions, the personnel of the departments, agencies and instrumentalities that receive financial support from the general fund, or otherwise depend on the fiscal authority of the central government, will be under the authority of the CFO.

Chapter 12. Medicaid investments and reform

12.1 Current State of Puerto Rico's Medicaid program

In 2019, ~37% of Puerto Ricans received their health coverage through the Commonwealth's state-run Medicaid program; this was the highest share of Medicaid/CHIP-funded health insurance coverage of any U.S. state.⁶² In addition to its large, covered population, Puerto Rico has lagged mainland U.S. jurisdictions in both health outcomes and access. Puerto Ricans face higher rates of chronic conditions like hypertension (12.4% above national median), diabetes (4.5% above national median), and asthma (1.6% above national median) than national averages.⁶³ Puerto Rico also has higher premature birth and infant mortality rates, and higher rates of adults reporting fair or poor health.^{64,65} At the same time, 72 of Puerto Rico's 78 municipalities are deemed "medically underserved areas," with 500 doctors leaving per year (pre-Maria). Puerto Rico has half the rate of specialists (e.g., emergency physicians, neurosurgeons) as compared to the mainland in critical fields.^{66,67}

Puerto Rico's Government-funded health plan, Vital, covers individuals through three primary funding sources: federally matched Medicaid funds, the Children's Health Insurance Program (CHIP), and the Commonwealth's self-funded insurance program for low-income adults who do not qualify for federally matched Medicaid. An additional ~8% of the Puerto Rican population receives some benefits from the Government as part of the Platino program, which supports Medicare Advantage recipients who also qualify for Medicaid (also known as "dual-eligible"). On November 15, 2020, the income requirements to qualify for Vital were increased temporarily until September 30, 2021. It is expected that approximately 200,000 individuals may become eligible for Vital during this period. If no new federal funds are approved by then, this population will be disenrolled.

Because federal Medicaid funding for US territories is currently subject to an annual cap, Medicaid expenditures eligible for federal matching exceed available funding without supplemental legislated sources. This makes Puerto Rico's Medicaid program very sensitive to rising healthcare costs. Since 2011, Puerto Rico has received temporary relief from rising healthcare costs through increased levels of federal reimbursement made available through the passage of the Affordable Care Act and the Bipartisan Budget Act of 2018. In December 2019, the Further Consolidated Appropriations Act was passed, which provided supplemental federal funding (up to \$5.7B total) to Puerto Rico's Medicaid program through September 30, 2021 (first quarter in FY2022). In addition, the law raised the FMAP—the portion of Medicaid expenditures that federal funds can cover—from the standard level of 55% to 76% for most populations. In response to the COVID-19 pandemic, the Families First Coronavirus Response Act was passed in March 2020, further increasing both the available federal funds (adding an additional \$183M) and the FMAP (increased an additional 6.2% for most populations). The available supplemental federal funds and higher FMAP will both return to standard levels in October 2021 without new federal legislation (see *Section 5.1.2* for more information on Medicaid federal funds). The 2021 Fiscal Plan assumes that as of federal fiscal year 2022, Puerto Rico will, consistent with President Biden's commitment for providing Puerto Rico parity in Federal Funding Programs, be treated

62 Kaiser Family Foundation, "Medicaid State Fact Sheets: Percent of People Covered by Medicaid/CHIP, 2019".

63 CDC (Centers for Disease Control and Prevention), "BRFSS Prevalence and Trends Data," 2019-2020. Behavioral Risk Factor Surveillance System.

64 Puerto Rico infant mortality rate is 6 per 1000 vs. US mainland 5.3 per 1000; premature birth rate is 11.8% vs. 9.6% in US mainland. "Puerto Rico," World Factbook (Washington, DC: CIA).

65 Kaiser Family Foundation, "Medicaid State Fact Sheets: Percent of People Covered by Medicaid/CHIP, 2019".

66 Areas with a shortage of personal health services, e.g., areas or populations that have too few primary care providers, high infant mortality, high poverty, and/or high older adult population.

67 HRSA Medically Underserved Areas (Accessed May 2020).

similar to other U.S. jurisdictions in terms of Medicaid funding and program requirement, which would mean unlimited federal financing for the program at an ~83% FMAP for its largest population. In return, Puerto Rico will provide all required benefits such as long-term care and Medicare Premium and Cost Share, which are currently not covered.

12.2 Medicaid reform measures

To attempt to resolve the Medicaid disparity in Puerto Rico, Governor Pierluisi's platform proposes the following efforts be undertaken.

- Continue the efforts before Congress to receive equal treatment through parity of funding in the Medicaid program for Puerto Rico, achieving, for the first time, the self-sustainability of the VITAL Plan
- Implement the strictest integrity and transparency measures in the Medicaid program to combat any fraud, abuse or waste of public funds, demonstrating to Congress our ability to make good use of funds and strengthen our legitimate claims for permanent parity
- Prioritize effective implementation of additional federal funds appropriated for federal fiscal year 2020 and 2021 to achieve the delivery of new benefits and critical sustainability measures in the Vital Plan and through this develop the credibility necessary to obtain the increased funding allocation prospectively
- Work to achieve the adjustment of the poverty level metric to increase Medicaid program eligibility in Puerto Rico to 200,000 new beneficiaries and with it a proportional increase in Medicaid allocation
- Analyze any federal public policy changes in the applicability of the Medicaid Drug Rebate Program and the Best Price policy in the financing of the VITAL Plan and the offering of drug benefits to VITAL patients

An estimated 340,000 Puerto Rico residents over the age of 65 are eligible for the Medicare (age-based) and Medicaid (indigent) programs. However, many do not have access to this benefit because they do not have the financial resources to contribute to Part B, a requirement for dual eligibility. Unlike the states, the government does not cover this contribution for residents of Puerto Rico. In addition to being a benefit for older and economically disadvantaged population, dual eligibility would significantly reduce the cost of the VITAL Plan and provide better resources to our providers and the health care economy. In light of this, Governor Pierluisi's platform proposes the following initiatives:

- Pursue Medicare Part B coverage for dual Medicaid and Medicare beneficiaries in the VITAL Plan's Medicare Platinum Program as provided in all states
- Introduce legislation at the federal level to identify funding and allocate parity for seniors to have their Part B coverage subsidized by the Federal Government and state government to increase participation of eligible people in the Medicare Advantage program (through the Medicare Platino Program), while reducing the costs of the VITAL Plan health program
- Similarly, there are other disparities in benefits when comparing health coverage in Puerto Rico and the other states. In light of the additional federal appropriations for federal fiscal year 2020 and 2021, it is imperative to consider adding new benefits to health coverage, such as: transportation to medical appointments, home and community-based health services, extended care services, immunizations for seniors, medical equipment, and lancets and band-aids for diabetic patients

The goal of the Puerto Rican public health insurance system is to fund high-quality health care services to all residents in need and, in doing so, cultivate a healthier population, especially as it relates to lowering outsized rates of chronic conditions. To ensure the system can continue to support the most vulnerable populations who rely on its services, **Puerto Rico will need to improve the efficiency and effectiveness of its health insurance plan by continuing to invest in reforms that allow coverage of all required benefits, provide adequate reimbursement to providers, and support the modernization of the healthcare infrastructure.**

This section outlines several categories of actions the Government will take to both to curb the growth rate in per capita health care expenditure as well as shift the health system overall toward higher-value care. In all the below required measures, the plan seeks to avoid reduction in service quality, and in many cases, reforms are expected to improve service quality for beneficiaries.

Puerto Rico's healthcare system has faced significant challenges from recent events. Unfavorable trends instigated by the hurricane (e.g., provider shortages, outstanding infrastructure needs) persist, and have been amplified by the earthquakes and COVID-19 pandemic. These circumstances make progress against healthcare measures challenging, and the availability of additional federal funding enable a more tempered path to achieving the target end-state for the healthcare system. To date, the Government has enabled savings through implementation of initiatives aimed at controlling healthcare cost inflation. These initiatives include the launch of the new, single-region managed care model and effectively managing the Prescription Drug List (PDL). These reforms are expected to continue to yield cost savings through greater competition, incentives to lower costs and reduction in administrative costs.

The measure savings in the 2021 Fiscal Plan are designed to lower premium expenditures across the multiple public health programs (namely Medicaid and CHIP). While the Government will continue to take actions to curb long-term costs, the 2021 Fiscal Plan surplus will only consider savings that accrue to the Commonwealth.

12.2.1 Medicaid reforms to improve program integrity

The 2021 Fiscal Plan includes savings on account of initiatives to reduce other forms of Medicaid fraud, waste, and abuse.

The US Government Accountability Office found evidence that MCOs have not consistently reported improper payments to providers billing to the system. Further, it found that many MCOs face conflicts of interest in finding and eliminating fraud.⁶⁸ Typical **fraud, waste and abuse reduction programs** in other state Medicaid programs and health insurers have been able to achieve 1-3% cost savings. These savings have been reached through: pre-payment review (e.g., reviewing claims before payment to identify outliers/issues); auditing and enforcement units to investigate suspicious behavior; advanced analytics capabilities to identify inefficient or fraudulent activities in post-payment review, such as identification of "impossible" utilization (e.g., billing for over 24 hours of service in one day) or frequently repeated, high value procedures; and long-term policy or organizational transformation. In addition, it is imperative for Medicaid programs to ensure coverage is offered only to eligible individuals through robust **enrollment verification**. Since 2014, states have relied on electronic sources to confirm information for purposes of determining Medicaid eligibility. However, GAO has found that inconsistencies and errors in eligibility determinations persist. Full compliance with Payment Error Rate Measurement (PERM) and Medicaid Eligibility Quality Control (MEQC)

68 GAO "Medicaid and CHIP Increased Funding in US Territories Merits Improved Program Integrity Efforts," April 2016.

requirements and establishment of an asset verification system that utilizes third-party data sources can strengthen enrollment verification.⁶⁹

To-date, Puerto Rico has made meaningful progress towards improving program integrity. This includes integration of ASES data with the Medicaid Management Information System (MMIS), establishment of a Medicaid Fraud Control Unit and Program Integrity Unit, establishment of a competitive process for Medicaid contracts, and improvement in enrollment verification through employer certification and Public Assistance Reporting Information System (PARIS) checks.

While Puerto Rico has taken steps towards improving its Medicaid Program integrity, opportunities for further improvement remain. Limited recoupments from MCO investigations suggest that additional opportunity remains. Best practices from other states indicate that additional program integrity activities can be developed in parallel to development of MMIS tools. For example, there is opportunity to leverage analytics vendors on a contingent bases to identify savings related to improper payments. Furthermore, enrollment verification can be improved by instituting an Asset Verification System and partnering with key out-migration states to conduct enrollment checks. Pursuant to the 2020 Further Consolidated Appropriations Act, Puerto Rico must continue to make progress to meet CMS's Payment Error Rate Measurement and Medicaid Eligibility Quality Control requirements.

12.2.2 Medicaid reforms to improve quality relative to cost

Pursuing value-based improvement initiatives with demonstrated success can help the Commonwealth “bend the curve” on healthcare inflation without jeopardizing – and in fact while improving –health outcomes across the system. Similar value-based programs have been piloted in other states, and typically have saved between 2-10% of costs included under the programs. In Puerto Rico, value-based reforms may result in lower-than-average savings due to the breadth of other simultaneous savings measures being implemented for Vital and challenges associated with recent natural disasters and the COVID-19 pandemic. Nevertheless, these structural changes to reimbursement and care delivery present the most viable path to long-term sustainability for the program.

There are several potential sources of value in Puerto Rico’s healthcare system. These sources of value are opportunities to reduce wasteful healthcare spending and increase efficiency while improving quality of care and health outcomes. One successful example is by reducing ER visits. Prior to Hurricane Maria and the reforms, Puerto Ricans utilized the ER three times as often as peers on the U.S. mainland, with estimates as high as 90% of ER visits occurring for non-emergency care that could be treated in lower cost settings.⁷⁰ From fiscal year 2017 to calendar year 2019 the ER PMPM cost decreased from \$12.13 to \$8.75. This reduction saves approximately \$40 million annually. Additional opportunity exists through reduction of inpatient length of stay. Puerto Rico’s inpatient length of stay was 1.5 times the US average in 2014.⁷¹ MCOs can incentivize reduced hospital readmissions and length of stay through improved discharge planning and increased staffing to manage weekend discharges. Hospitals can improve quality of care and long-run costs by reducing hospital readmissions. Hospital readmissions occur when patients are discharged from hospitals but must return for additional treatment for the same condition. This can occur when patients are not adequately prepared to return home due to lack of education, lack of access to follow-up care, challenges with

69 GAO “Medicaid Eligibility: Accuracy of Determinations and Efforts to Recoup Federal Funds Due to Errors,” January 2020.

70 JEL Consulting analysis (Dec 30, 2106) of ASES data and Puerto Rico Community Survey, Public Use Microdata, 2014. Estimates exclude Platino beneficiaries.

71 As of 2014. JEL Consulting analysis (Dec 30, 2106) of ASES data and Puerto Rico Community Survey, Public Use Microdata, 2014. Estimates exclude Platino beneficiaries.

prescription drugs, etc. Readmission rates at hospitals in Puerto Rico are higher than the national average. Savings can be achieved by incentivizing hospitals to minimize readmissions.

Value-based payment models are an effective tool to capture these sources of value and incentivize providers to fully treat patients in more efficient ways. Pursuant to this measure, ASES has begun development of a Diagnosis Related Group (DRG)-based payment model. Under a DRG-based payment model, providers are reimbursed a fixed amount to fully treat a patient with a given medical condition. DRG-based payment models help control medical costs by incentivizing providers to deliver cost-effective care without sacrificing quality. In addition, these payment models improve the effectiveness of Medicaid service delivery by standardizing the measurement of patient acuity across providers and reducing the administrative burden associated with reimbursements, etc. ASES has begun using a case mix adjustment that adjusts the payment to each hospital from the inpatient hospital funding pool based on the severity of conditions that each hospital treats, relative to each other. This is a first step towards moving the Puerto Rico hospital system to a DRG based payment. Successful actualization of savings from this effort is necessary for the Government to fund the long-term health needs of Puerto Rico.

There are several, additional value-based payment models that can be implemented to achieve cost savings. Best practice value-based payment models from other managed care settings include direct pay-for-performance quality bonuses, providing special incentives to care for members with high-cost needs, such as behavioral health, etc. New approaches that emphasize care coordination and align incentives between patients, providers, and payors can produce improvements in health outcomes while lowering costs. Care coordination models like patient centered medical homes – which empower primary care providers to work closely with patients and manage treatment plans across multiple care providers – have been quite effective at improving outcomes for members with chronic conditions.⁷² Given the preponderance of chronic conditions and potential rising behavioral and mental health needs in the wake of Hurricane Maria, better access and coordination of mental health services will become increasingly important.⁷³

12.3 Medicaid investments

Puerto Rico’s healthcare system has experienced significant strain stemming from the hurricane, earthquakes, and COVID-19 pandemic. These events are expected to have amplified provider shortages and create increases in demand for health services, particularly behavioral health care. Given these turbulent circumstances and the uncertain outlook with respect to the COVID-19 pandemic, it is prudent to make incremental investments in the health system. Such investments are enabled by federal funding made available through the 2020 Further Consolidated Appropriations Act and the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). As a result, the Government has made certain priority investments that provides Hepatitis C drug coverage and increasing reimbursement rates to specialty and primary care providers and hospitals. In addition, the Government will continue to invest newly awarded federal funds by providing required benefits, further increasing provider reimbursements, permanently increasing income qualification threshold, and improving program integrity.⁷⁴

72 Patient-Centered Primary Care Collaborative, “Benefits of Implementing the Primary Care Medical Home: A Review of Cost & Quality Results, 2012” (Sept 2012).

73 Thomas Huelskoetter, Center for American Progress, “Hurricane Katrina’s Health Care Legacy” (August 15, 2015).

74 <https://www.macpac.gov/topics/long-term-services-and-supports/>. *** THIS FOOTNOTE IS ONLY FOR “Provide coverage for long term services and supports (LTSS) (approximately \$1 billion annually): LTSS is a required Medicaid benefit that is currently not covered due to the extremely high cost. LTC benefits provide institutional and at home services to the aged and disabled population, which are some of the most expensive beneficiaries.”

Increased provider reimbursement rates

Reimbursement rates for Government Health Plan (GHP) providers lag those of Medicaid programs in other states and territories. For example, from July 2016 to July 2017 primary care services were reimbursed at 19% of the Puerto Rico Medicare fee-for-service rate, while these services are reimbursed at 66% of the Medicare rate nationally. Also, maternity services were reimbursed at 50% of the Puerto Rico Medicare fee-for-service rate while these services are reimbursed at 81% of Medicare rate nationally. Low reimbursement rates place pressure on providers and may lead to shortages, lack of access to certain specialty services, and lengthy wait times. From today through September 30, 2021, ASES will increase provider reimbursement rates as follows:

- **Establish a 70% of Medicare reimbursement floor for outpatient physician services:** Pursuant to a provision in the 2020 Further Consolidated Appropriations Act, ASES has established a reimbursement floor for physician services set at 70% of the Medicare fee-for-service rate. The costs associated with the investment will be included in the Managed Care Organization PMPM capitation rate. In turn, the MCOs will be contractually obligated to reimburse all contracted providers at the rate of at least 70% of the Puerto Rico Medicare fee schedule.
- **Increase sub-capitation payment for primary care physician (PCP) services:** Almost all primary care services are paid through sub-capitation arrangements, wherein MCOs pay Primary Medical Groups (PMGs) a fixed, monthly rate per member treated. To improve access to primary and preventive services, ASES has included a 10% increase in the PMPM sub-capitation rate paid to PMGs for contract year 2020-2021.
- **Increase reimbursement rates for hospitals:** According to CMS Hospital Cost Reports, over 50% of Puerto Rico hospitals reported net losses. Given the high portion of the population covered by Medicaid, Puerto Rico hospitals are disproportionately affected by reimbursement rates of the Medicaid program, which are lower than those of most other payers. These conditions jeopardize the ability for hospitals to operate and re-invest in their infrastructure. To support the ability of hospitals to meet the needs of Puerto Rico, ASES will increase reimbursement rates. Specifically, ASES has established a funding pool that provides supplemental payments to hospitals in addition to their regular reimbursement. The reimbursement to each hospital will be adjusted based on the acuity of cases that each hospital has relative to each other, similar to a DRG payment system methodology.
- **Hepatitis C drug coverage:** Puerto Rico's Medicaid plan did not previously provide coverage for drugs that cure the Hepatitis C virus. There are approximately 14,000 Puerto Ricans that are eligible for treatment and could be cured by making these drugs available to them. Granting coverage for these drugs will significantly increase the quality of lives for affected individuals. Furthermore, in the long term, it is estimated that savings can be achieved due to the avoidance of costs related to the treatment of Hepatitis C virus such as decompensated cirrhosis and liver transplants. This benefit has been available since March 2020.
- **Medicaid IT:** Funding for capital expenditures and operational support to enable ASES to improve and modernize technology for eligibility processing and enrollment verification, and invest in analytics to identify fraud, waste, and abuse, claims cost optimization opportunities, and inform value-based program design.
- **Provide coverage for long term services and supports (LTSS):** LTSS is a required Medicaid benefit that is currently not covered due to the extremely high cost. LTC benefits provide institutional and at home services to the aged and disabled population, which are some of the most expensive beneficiaries. The types of services offered vary widely and include nursing home and community-based services (HCBS). In Puerto Rico, the long-term care infrastructure is not as developed as in the States in large part because Medicaid does not cover this benefit. Adding LTSS to the coverage will improve the care, treatment, and quality of life of the approximately 700,000 elderly and disabled persons that reside on the island. This initiative represents approximately ~\$1.1 billion in incremental annual spend by FY2023, growing at the healthcare inflation rate offset by the Puerto Rico population decrease.

- **Payment of Medicare premiums for dual-eligibles:** Medicaid programs are required to cover the cost of Medicare premiums and deductibles for their Medicare and Medicaid beneficiaries. Puerto Rico plans to cover these costs for the approximately 360,000 dual-eligibles in the program. In most cases, these beneficiaries pay these costs out-of-pocket, which can be upwards of \$100 monthly. Payment of these premiums will provide necessary direct relief to this vulnerable population. This initiative represents approximately ~\$750 million in incremental annual spend by FY2023, growing at the healthcare inflation rate offset by the Puerto Rico population decrease.
- **Coverage of other required benefits:** Puerto Rico currently does not cover all Medicaid required benefits, such as non-emergency medical transportation (NEMT) and diabetic supplies. The goal is to provide all required benefits to the Medicaid population if federal funding allows.

Chapter 13. Tax compliance and fees enhancement

13.1 Current state and future vision for tax environment

Puerto Rico has historically struggled with a tax system that suffers from structural complexity and inadequate enforcement. There have been at least 11 major revisions to Puerto Rico's tax code since 1994, including at least six adjustments since 2013.⁷⁵ Top marginal tax rates are high relative to US federal and state taxes. Much of the Government's revenue is highly concentrated in collections from a handful of multi-national corporations. The Government has also issued an assortment of credits, deductions, and incentives that add to the system's complexity and further erode the tax base. Furthermore, audit and enforcement activity in recent years has been limited, which creates risks of increased levels of non-compliance.

Due to its compliance and collections issues, the Commonwealth has not been able to collect as many revenues from taxes as it should each year.

In response to these challenges, the Government has taken actions to improve tax compliance. It has taken steps to improve information reporting to better detect under-reporting of income and over-usage of deductions and credits, notably through recent changes to information reporting requirements included in Act 257-2018. These changes create greater interdependencies among taxpayers and the information they are obligated to report, which is expected to enable greater oversight and verification of the information being reported to the Government. Enhanced usage of data can help Hacienda better isolate risk and focus its compliance and enforcement resources. It is driving improvements in its culture and organization to boost enforcement capabilities, and digitizing the process of filing taxes, to lighten the burden of compliance on taxpayers.

With the publication of the first Tax Expenditure Report in September 2019, policymakers now have the data necessary to review, assess, and adjust the use of individual tax expenditures to ensure that these foregone revenues are leading to positive economic development on the Island.

13.2 Administrative tax initiatives to increase revenue collections

Through implementation of administrative tax reform and realization of measures included in prior fiscal plans, the Government has captured significant incremental revenues, which are implicit in the baseline FY2021 general fund revenue forecast.

13.2.1 *Improve compliance rate*

The Government has achieved a target 5% net uplift in annual revenues due to enhanced compliance across the major tax lines (personal income tax, corporate income tax, and SUT) – inclusive of implementation costs. This improvement is evidenced by continued

⁷⁵ Reforms include: Act 40-2013, the "Tax Burden Redistribution and Adjustment Act;" Act 120-2014, the "Small and Medium Business Job Generation and Retention Act;" Act 72-2015, the "Adjustments to the Internal Revenue Code of 2011;" Administrative Orders 2017-01 and 2017-05; and Act 257-2018, the "2018 Puerto Rico Tax Reform Act."

outperformance in these categories and driven by the successful implementation of SURI. The impact of increased compliance is in-line with improvements seen in other tax transformations.⁷⁶

Hacienda is taking a variety of initiatives that will boost voluntary compliance. The goal is to reduce the cost of compliance while simultaneously raising the cost of non-compliance, through a combination of an increased likelihood of being caught while not paying taxes owed and more effective and enforceable penalties.⁷⁷

- **Use new systems and processes to identify and remediate non-compliance:** Hacienda has taken steps to make it harder to abuse deductions and credits to avoid tax liability, for example by only allowing taxpayers to claim certain deductions and exemptions if their return is prepared by a certified public accountant following agreed upon procedures.
- **Reduce the complexity of the tax system and process of filing taxes** to make it easier for individuals and businesses to pay their taxes correctly. Improving the process for filing and paying taxes is critical for improving ease of doing business, but it also helps boost voluntary compliance.
- **Improve use of data and analytics to address non-compliance:** Small and medium taxpayers account for a significant share of the unpaid and underpaid taxes, but only a tiny fraction of these taxpayers receives full-scale audits due to the significant time and cost investment needed. While a traditional IRS audit costs an average of \$2,278 per case, automated notices or letters can be executed for \$52 to \$274 per case.⁷⁸ Hacienda is receiving increasing filings of information returns that can be used to better identify risk and focus compliance resources. Implementing data-driven, tiered compliance approaches over time will enable Puerto Rico to reach a significantly larger share of non-payers.
- **Collecting SUT on Internet sales:** Nationally, the percentage of taxpayers voluntarily reporting and paying sales and use taxes on their income tax forms ranges from 0.2% to 10.2%, while nearly 80% of Americans shop online.^{79,80} Mainland states have taken steps to improve sales tax collections on online sales through legislation, as well as voluntary agreements with major online retailers.⁸¹ In its 2018 *Wayfair* decision, the US Supreme Court further provided mainland states with parameters under which sales taxes could be levied on out-of-state sellers. Given these trends, the Government should also be working to capture SUT on a much larger share of Internet sales. Hacienda has announced agreements with some online retailers to charge Puerto Rico SUT on Internet sales of goods.⁸² With Internet sales growing at ~15% annually, and growth expected to accelerate further as the COVID-19 pandemic makes the internet a critical component of consumer purchasing habits, Internet sales tax presents an even more important opportunity going forward.

The targeted impact from these compliance related activities has been achieved and is reflected in the baseline general fund revenues; however, Hacienda will continue to pursue additional revenues through increased compliance.

76 Analogous case studies include Panama, Jamaica, and Spain, which saw 1.0 to 2.5 percentage point increases in tax ratio relative to GDP through comprehensive tax overhauls, which included compliance initiatives.

77 Xenia Velez presentation to the Oversight Board (Nov. 30, 2017)

78 IRS Enforcement Results, TIGTA Filing Season Audit, IRS Taxpayer Advocate, Team Analysis, GAO.

79 "Use Tax Collection on Income Tax Returns in Other States" Research Department of Minnesota House of Representatives, April 2015. <http://www.house.leg.state.mn.us/hrd/pubs/usetax.pdf>.

80 Tech Crunch, 2016.

81 Voluntary agreements occur when corporations agree through individual negotiations with states to collect and remit sales tax directly to the state.

82 Caribbean Business, "Amazon to charge Puerto Rico sales tax".

13.2.2 Right-rate other taxes and fees

The Government has implemented various initiatives, starting in FY17, to enhance revenue through right-rating taxes and fees related to gaming machines, tobacco products, Airbnb taxes, medical marijuana, and other licenses and fees. The impact of these initiatives is implicit within the FY21 baseline.

13.3 Implementation and enforcement of revenue measures

To date, Hacienda has made important progress towards deploying SURI, its integrated tax system. The benefits of the SURI platform include improved filing and payment capabilities, digital workflows, and integration of previously disparate data sources. These features are expected to continue to improve Hacienda's ability to serve taxpayers and enhance its compliance capabilities. Hacienda has also begun to make use of new information reporting and withholding requirements to limit the structural opportunities for non-compliance (e.g., through the use of alternative minimum taxes and limitations of deductions where there is no corroborating information reporting).

13.3.1 Creation of a tax expenditure report and regular reporting

In order to provide a critical element of fiscal responsibility and transparency, the Government will regularly produce a tax expenditure report, which will include a comprehensive list of revenue losses attributable to provisions of the Puerto Rican tax code that deviate from the tax structures benchmark law. Having a clear and accurate understanding of what the Government spends through tax expenditures is critical to ensuring the expenditures are continuing to contribute to economic growth and opportunity.⁸³

the Government published its inaugural Tax Expenditure Report in September 2019 for tax expenditures associated with tax year 2017. For the first time in Puerto Rico's history, taxpayers and the Government now have better visibility into the full scope of tax expenditures being offered, together with a description and approximate cost of each expenditure. Additional revisions to the tax expenditure reporting are in process by the Government in order to continue to improve the process.

13.3.2 Tax incentives code reform

The current tax incentives code structure a fiscal cost in excess of \$400 million. Past studies, based on limited available economic data, have indicated that while some tax incentives led to positive returns on investment, many others do not yield similar results.

That is what led the Commonwealth to enact Act 60-2019 (the "Puerto Rico Tax Incentives Code" or "Incentives Code"), which amended the tax incentives code and adopted a new legal and administrative framework to normalize the way in which new incentives are created, approved, processed, and monitored. Existing incentive laws were repealed and replaced by similar incentives in Act 60-2019.

To evaluate the fiscal benefit from each incentive, the legislation uses a Return on Investment ("ROI") approach combined with an assessment of fiscal multipliers to prioritize high value-added incentives relative to those that do not generate sufficient economic return. the purpose of the Incentives Code is to measure the ROI of tax and economic incentives by grouping them

⁸³ Tax Policy Center, Urban Institute & Brookings Institution, "State Income Tax Expenditures".

under a transparent and uniform code, not to arbitrarily reduce, cap, or eliminate specific incentives.

Through the Incentives Code, the term, rate, and characteristics of incentives offered are harmonized across industries and credits. The Incentives Code also creates a centralized Incentives Office for Businesses in Puerto Rico at DDEC and establishes an Incentives Concession Portal to centralize, standardize, and streamline the processes related to the application and approval of decrees, cash grants, tax credits, subsidies, and other incentives.

Act 60-2019 also required the public disclosure of beneficiaries of certain tax expenditures. In accordance with that requirement, DDEC disclosed (on January 30, 2020) that 8,364 companies and individuals received certain tax incentives. The online database offers the name of the grantee, the type of benefit, and the decree's issue date. At the moment, DDEC released the relevant information for recipients that receive benefits from the following Acts: Act 14-2017 (Physician Retention); Act 20-2012 (Exportation of Services); Act 22-2012 (Investor Relocation); Act 273-2012 (International Financial Center Regulatory Act); and Act 27-2011 (Film Production). DDEC subsequently released additional data on February 11, 2020, disclosing recipients of the following tax expenditures: Act 73-2008 (Economic Incentives for the Development of Puerto Rico Act); and Act 83-2010 (Puerto Rico Green Energy Incentives Act).

Many provisions of Act 60-2019 require the drafting and approval of regulations prior to their implementation.⁸⁴

13.3.3 Principle of Revenue Neutrality

Puerto Rico needs to drive toward more formality and increased compliance within the tax base, but it cannot lose revenues in the process. Therefore, any tax reform or tax law initiatives that the Government undertakes or pursues during a year within the 2021 Fiscal Plan period will be revenue neutral, that is, all tax reductions must be accompanied by specific, offsetting revenue measures of the same amount that are identified in the enabling legislation.

Chapter 14. Municipal services reform

14.1 Current state

Puerto Rico's 78 municipalities are also recipients of Commonwealth appropriations. Prior Fiscal Plans reduced Commonwealth appropriations to municipalities. In FY2018, the total municipal appropriation was \$220 million (a reduction of \$150 million relative to the prior year). In FY2019, it was reduced to \$176 million, and in FY2020, as stipulated in the 2019 Fiscal Plan, it was further reduced to \$132 million. However, 2021 Fiscal Plan does not include further cuts to the municipalities, as outlined in *Chapter 1*.

Municipalities should consider the pursuit of consolidation of services across multiple municipalities to enable better and more efficient services for Puerto Rico residents. Consolidation, with appropriate process efficiencies, has the potential to significantly reduce costs by leveraging scale, especially in areas of services provided directly to residents, such as garbage disposal and maintenance of municipal buildings and roads.

⁸⁴ Pursuant to PROMESA section 204(b)(4) and the Oversight Board's policy with respect thereto, proposed rules, regulations, administrative orders, and executive orders covered by said policy, including all regulations under Act 60-2019, must be submitted to the Oversight Board before being issued to ensure compliance with the certified Commonwealth Fiscal Plan.

14.2 Disaster recovery and the COVID-19 crisis

14.2.1 Accelerating post-disaster recovery at municipalities

Puerto Rico has experienced historic and unprecedented disasters since 2017. The impact of Hurricanes Irma and Maria, as well as a magnitude 6.4 earthquake on January 7, 2020 (and the subsequent aftershocks), resulted in significant damage to the infrastructure and economy, and prompted material out-migration. The Federal Government has supported post-hurricane reconstruction in the municipalities primarily through FEMA’s Permanent Work (Categories C-G) Small Projects and Community Disaster Loans (CDLs). Small Projects are defined as those with total project costs of up to \$123,100 for Permanent Work Categories C-G. As of May 18, 2020, 1,224 projects have been obligated to municipalities, totaling ~\$48.9 million, of which ~\$33.5 million has been disbursed. In addition, 3,285 Small Projects are currently in the project formulation stage, with a total approximate cost of \$152 million. CDLs are provided to municipalities that have suffered a substantial loss of revenues as a result of a disaster and that can demonstrate a need for federal financial assistance to perform critical functions such as payroll, supplies, and maintenance materials related to disaster operations. 76 of the 78 municipalities have received nearly \$300 million from the Federal Government to make up for lost revenues due to the Hurricanes in the form of CDLs. Municipalities and the people of Puerto Rico have also received disaster funding through Individual Assistance programs, Small Business Administration Loans, Department of Housing CDBG-DR programs, and Department of Transportation funding.

On December 7, 2019, the Oversight Board approved the Government’s request to establish a “State Recovery Fund” that would fund advances to eligible Small Projects under the FEMA Public Assistance program, which many municipalities required due to a lack of liquidity.⁸⁵ The State Recovery Fund was financed solely from a reprogramming of the \$100 million FY2020 certified budget appropriation under the custody of OMB designated as “Cost share of public assistance” and is to be used only for Small Projects (as defined above). The Oversight Board also included several requirements from the Government as a precondition to approval of this State Recovery Fund. Since the establishment of this State Recovery Fund, COR3 has informed the Oversight Board that \$92.5 million would be returned to OMB given other mechanisms have been put in place to expedite Small Projects and the funds are no longer required by the municipalities.⁸⁶

14.3 Vision and reform needed to transform municipal services

Municipalities are the first line of response for the people of Puerto Rico. The solvency and fiscal viability of each of the 78 municipalities is important for the continuity of essential services, such as health, security, housing, garbage collection, maintenance of streets and public areas, promotion of commercial activity, promotion of culture, sports, and entertainment. To this end, the Government will use available resources to achieve efficiencies and bring funds to the municipalities through the following initiatives:

- Provide assistance to municipalities in obtaining recurring federal funds such as Moving Back to Work, Pay for Success, TIFIA and Build Grants, among others
- Implement a less bureaucratic and centralized system of government to give more power and resources to municipalities. The Administration will evaluate all services that municipalities can provide more efficiently, either individually or through consortiums

⁸⁵ Oversight Board letters dated December 7 and December 14, 2019.

⁸⁶ COR3 letter to the Oversight Board dated April 14, 2020.

- Promote that reconstruction projects be handled by the municipalities without the intervention of the central government bureaucracy
- Establish a public policy that will give priority to the municipalities in relation to the use and development of schools closed and other structures disused by the central government
- Support municipal consortiums and shared services in key areas such as garbage collection, public safety, finance, accounting, and human resources
- Streamline processes to identify and make available non-revenue-generating, idle state government properties for economic development and municipal services, such as permanent shelters, and to establish agreements for the management of recreational facilities, lodges, and resorts
- Promote an accelerated approval program for the transfer of disused central government properties to earthquake-affected municipalities in the south to expedite the replacement of affected schools and structures
- Support and expedite the disbursement of funds and the development of recovery and reconstruction projects (FEMA, HUD, CDBG-DR, among others) of the municipalities
- Seek options to the decapitalization of the Equalization Fund whose support disappears by 2024 as a result of the fiscal plan
- Promote the reengineering and modernization of the systems and services of the Municipal Tax Collection Center (CRIM) to increase efficiency in its services and increase revenue collection through the use of technology and outsourcing of resources
- Support recovery programs to help municipalities affected by the 2020 earthquakes
- Facilitate permits, economic activity, and job creation to increase municipal revenues. To this end, the government should ensure an economic diversification plan through the retention, expansion, and new investment of commercial activity
- Encourage municipal public-private partnerships for strategic functions, services, and projects of regional impact, with a focus on job creation and increased revenues
- Promote the development of broadband and 5G telecommunications infrastructure for greater citizen interconnectivity and establish the basis for the development of innovative municipal services and the elements, capabilities, and business promotion of so-called Smart Cities

This Administration is committed to providing the necessary mechanisms to strengthen municipalities within a framework of partnership with the Central Government. After the emergencies experienced during the last few years due to hurricanes, earthquakes and pandemics, the municipalities were the executing arm of the vast majority of the initiatives to directly respond to the needs of the victims, on many occasions with limited resources. This Administration will have a genuine commitment with the municipalities of Puerto Rico and proposes the following initiatives as part of the public policy.

- Create the position of Assistant Secretary of Municipal Affairs at La Fortaleza, providing him/her with the power and the necessary tools to work together with the secretaries and agency heads in favor of the municipalities and their residents
- Work on the decentralization of those services currently provided by the central government that can be provided more efficiently and economically by the municipalities
- Establish a program of economic compensation for the expenses incurred by the

municipalities in the provision of services that correspond to the central government, such as the maintenance of state highways, schools, sports facilities, and others

- See to it that all legislation passed by the central government respects municipal autonomy and does not burden municipal budgets
- Work to ensure that the central government's budget includes the necessary resources to free municipalities from contributions to the Retirement Systems and to the Government's Health Plan
- Give priority in granting leasing contracts for disused schools to those municipalities that wish to convert them into shelters or develop any economic development projects, community or educational projects and service programs
- Promote collaboration agreements in order to transfer to the municipalities the control and administration of recreational facilities, spas, inns, lodges, vacation centers and any other facilities of the same nature that they may manage and maintain
- Promote the creation of inter-municipal consortiums to develop micro-energy networks, permitting offices or any other regional economic development project. Likewise, the Government will encourage the creation of inter-municipal consortia in municipalities with a population of less than 50,000 inhabitants for the purpose of being direct recipients of federal funds, such as CDBG, and will provide the necessary tools for the achievement and fulfillment of their objectives

A consolidated municipal service structure could enable the delegation of certain Commonwealth responsibilities to local governments. Such a model could yield municipal and Commonwealth savings, and a portion of those savings could be reinvested back into the municipalities where savings are realized.

In addition, a more integrated government structure could help implement locally based economic development strategies, which are more viable at a regional level than on an individual municipality basis.

14.3.1 Incentivizing consolidation of services

To further incentivize service consolidation, the 2021 Fiscal Plan lays out a set of voluntary options for municipalities to consider. By consolidating services, municipalities will be able to significantly reduce costs. Under this approach, municipalities that voluntarily choose to consolidate services will be eligible to receive a one-time financial incentive upon certification of such action by the Oversight Board. To fund this initiative, the 2021 Fiscal Plan sets aside \$22 million in each fiscal year through FY2025 for distribution among municipalities that complete service consolidations, as confirmed by the Oversight Board. The amount distributed will be determined in coordination between AAFAF and the Oversight Board and will depend on the size of the municipality and the scale of service consolidation. Property tax reform

CRIM plays an important role in supporting Puerto Rico's municipalities in their economic and social development by ensuring an efficient process to collect and distribute real and personal property tax revenues, which are an important revenue stream for municipalities. In FY2020, property taxes represented approximately 29% of the aggregate general fund budget for municipalities.

Historically, the taxable value of real and personal property has been significantly reduced by tax exemptions and exonerations. In FY2019 for example, more than 50% of the real and personal property tax base was eliminated through these exemptions and exonerations. In addition, there is a backlog of real properties not yet appraised, and collection rates for current

year real property tax billings are well below comparable jurisdictions at approximately 68%. This has resulted in a large accounts receivable balance. Therefore, it is essential that CRIM seize all opportunities to maximize property tax collections to improve municipal revenues.

In partnership with the municipalities, CRIM should implement measures to capture unrealized property tax revenues by increasing tax compliance and improving overall collection rates. CRIM should also update the tax roll to include the tens of thousands of non-registered properties and home improvements. Additionally, CRIM should undergo an operational transformation centered around the replacement of outdated and inefficient applications and hardware and the establishment of a data driven culture. Based on implementation planning discussions with CRIM management, CRIM estimates these initiatives could produce:

- \$70 million of additional annual revenue from raising real property tax compliance from 68% to 76%.
- \$118 million of additional annual revenue from registering properties and home improvements not on the tax roll.
- Sell the accounts receivable portfolio.

Additional revenue-enhancing measures are identified in CRIM's Fiscal Plan

PART VII. Conclusion

The people of Puerto Rico have undoubtedly endured significant hardships over the past several years. In the nearly four years since Congress passed PROMESA, Puerto Rico has been challenged by the most damaging hurricanes in U.S. history and the strongest earthquakes in the Caribbean in over a century. These natural disasters have further complicated an already decades-long, Island-wide recession marked by significant population loss.

Most recently, the COVID-19 pandemic has tested Puerto Rico and the world, leaving in its wake profound uncertainty about the short- and long-term effects of the disease on human society, health, and business. COVID-19 has upended the way people work, interact, and learn, and will fundamentally change future business practices and public policies. In response to the pandemic, the Government took swift action to flatten the curve and protect its residents. These actions included stringent social distancing measures and significant investment that was, and continues to be, needed to minimize the impact of the pandemic on the Island and its people. While significant uncertainty remains, progress in contact tracing and testing as well as the recent authorization and distribution of vaccines has garnered hope for a return to normalcy.

Amid these crises, the Government has worked tirelessly with the Oversight Board to advance a Title III Plan of Adjustment. Restructuring Puerto Rico's debt is a critical step towards regaining access to the capital markets, increasing private investment, creating jobs, and improving the living conditions for the people of Puerto Rico. In February 2021, the Oversight Board entered into a Plan Support Agreement with a significant group of creditors that would materially reduce the Government's debt burden. As currently constructed, the Government does not support this agreement because it believes certain cost-cutting measures would unfairly harm a group of Puerto Rico's most vulnerable citizens; specifically, the Government's pensioners. However, the Government remains hopeful that a consensual plan can be reached, and that the Commonwealth can, in short order, emerge from its Title III proceedings with a more balanced and sustainable balance sheet that is fair to all stakeholders.

There is no doubt that the road to recovery in Puerto Rico is one that will continue to be challenging. Yet despite its many historical challenges, Puerto Rico remains optimistic, determined, and full of potential. The Government will continue to pursue outcomes that are fair and just to all constituents. By focusing on transparency, responsiveness, efficiency and execution, this administration is confident that it can, and will, govern with excellence and improve the quality of life for all Puerto Ricans.

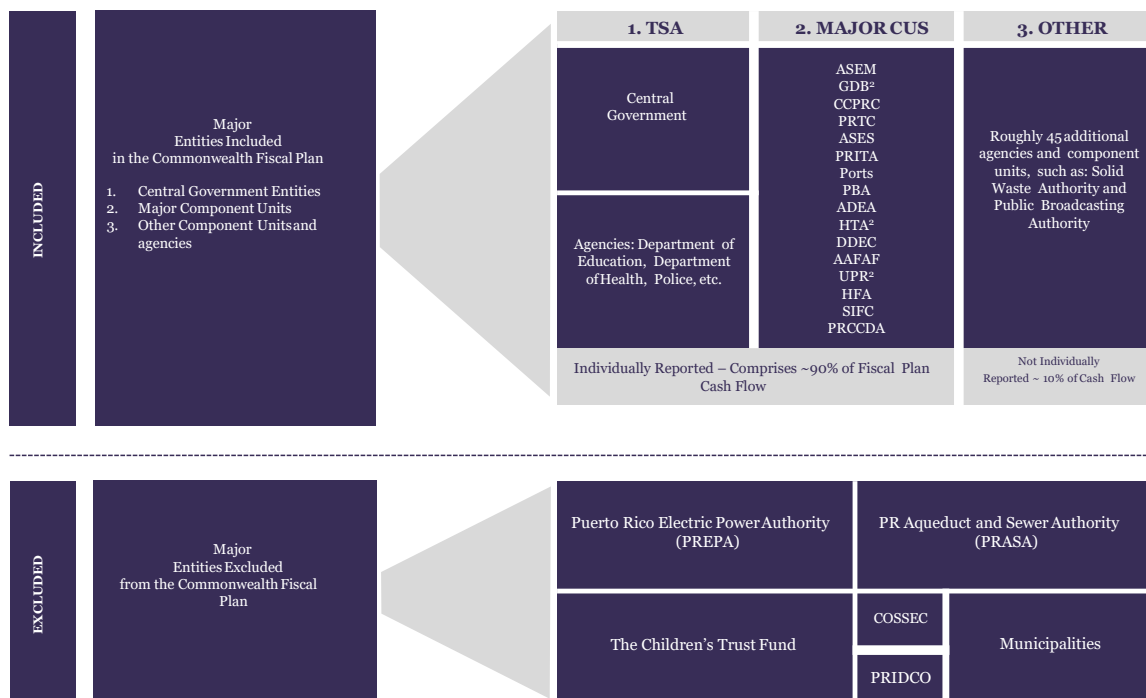
Appendix

Chapter 15. Model presentation

15.1 Overview of entities covered by and excluded from the 2021 Fiscal Plan

The 2021 Fiscal Plan addresses the finances of central government agencies, component units, and other agencies. Agencies for which an independent Fiscal Plan is being developed have not been consolidated into the 2021 Fiscal Plan and are only represented to the extent they impact the Commonwealth. It is important to note that PRIDCO has been removed from the 2021 Fiscal Plan, which is a change relative to prior Fiscal Plans and therefore may make some numbers incomparable.

EXHIBIT 34: MAJOR ENTITIES INCLUDED IN AND EXCLUDED FROM THE 2021 FISCAL PLAN



(1) Major CUs include the following IFUCs: ASEM, ASES, PRITA, PORTS, PBA, ADEA, AAFAP, HFA, SIFC, PRCCDA. (2) GDB, HTA, and UPR have separate and apart fiscal plans from the Central Government; HTA and UPR receive General Fund appropriations.
 Note: Housing Finance Authority and resources from the Cap Funds (money transferred by HUD for financing projects and repayment of bonds) are not contemplated in the New Fiscal Plan.

EXHIBIT 35: LIST OF ENTITIES COVERED BY THE 2021 FISCAL PLAN

- Office of the Comptroller
 - General Court of Justice
 - Traffic Safety Commission
 - Environment Quality Board
 - Office of the Governor
 - Office of Management and Budget
 - Planning Board
 - Emergency Management and Disaster Admin Agency
 - Office of the Commissioner of Insurance
 - Department of State
 - Department of the Treasury
 - Hacienda
 - Commonwealth Election Commission
 - Federal Affairs Administration
 - Office of Admin and Transportation
 - General Services Administration
 - Investigation, Prosecution and Appeals Commission
 - Industrial Tax Exemption Office
 - Civil Rights Commission
 - Department of Justice
 - Puerto Rico Police
 - Puerto Rico Firefighter Corps
- Puerto Rico National Guard
 - Department of Public Safety
 - Department of Transportation and Public Works
 - Department of Natural and Environmental Resources
 - Department of Agriculture
 - Citizen's Advocate Office (Obudsman)
 - Cooperative Development Commission
 - Public Services Commission
 - Department of Labor and Human Resources
 - Labor Relations Board
 - Department of Consumer Affairs
 - State Insurance Fund Corporation (SIFC)
 - Department of Health
 - Office of the Financial Institutions Commissioner
 - Department of Housing
 - Automobile Accident Compensation Admin (ACAA)
 - Department of Education
 - Institute of Puerto Rican Culture
 - Department of Sports and Recreation
 - Horse Racing Industry and Sport Administration
 - Medical Services Administration (ASEM)
 - Mental Health and Addiction Services Administration
 - Women's Advocate Office
- Legislative Assembly
 - Industrial Commission
 - Public Housing Administration
 - School of Plastic Arts
 - Dept. of Economic Development and Commerce
 - Veterans Advocate Office
 - 9-1-1 Services Governing Board
 - Department of the Family
 - Families and Children Administration
 - Child Support Administration
 - Vocational Rehabilitation Administration
 - Admin for Socioeconomic Develop of the Family
 - Natural Resources Administration
 - Department of Correction and Rehabilitation
 - Institutional Trust of the National Guard of Puerto Rico
 - Parole Board
 - Telecommunication's Regulatory Board
 - Elderly and Retired People Advocate Office
 - Advocacy for Persons with Disabilities of the CW of PR
 - State Historic Preservation Office
 - Infrastructure Financing Authority
 - Public Buildings Authority (PBA)
- Land Authority of Puerto Rico
 - Company for the Integral Development of Cantera's Peninsula
 - Ports Authority
 - Land Administration
 - Tourism Company
 - Solid Waste Authority
 - Culebra Conservation and Development Authority
 - Health Insurance Administration (ASES)
 - PR and the Caribbean Cardiovascular Center Corp
 - Institute of Forensic Sciences
 - Musical Arts and Stagecraft Corporation
 - Fine Arts Center Corporation
 - Office of Government Ethics
 - Economic Development Bank
 - Public Broadcasting Corporation
 - Farm Insurance Corporation
 - Special Independent Prosecutor Panel
 - Contributions to Municipalities (CRIM)
 - AFICA
 - Conservatory of Music
 - Correctional Health
- Health Advocate office
 - Housing Financing Authority (HFA)
 - Port of the Americas Authority
 - Administration for Integral Development of Childhood
 - Puerto Rico Trade and Export Company
 - Martin Peña Canal ENLACE Project Corporation
 - Roosevelt Roads Naval Station Redevelopment
 - Institute of Statistics
 - Office of the Inspector General
 - Permit Management Office
 - Public-Private Partnership Authority
 - Agricultural Enterprises Development Admin (ADEA)
 - Puerto Rico Education Council
 - Public Service Appeals Commission
 - Office of the Electoral Comptroller
 - Puerto Rico Integrated Transport Authority (PRITA)
 - Ponce Port Authority
- Energy Commission
 - Energy Affairs Office
 - Center for Research, Education and Medical Services for Diabetes
 - Bosque Modelo de Puerto Rico
 - Fiscal Agency and Financial Advisory Authority (AAFAF)
 - Convention Center District Authority (PRCCDA)
 - Socio-Economic Development Office
 - Government Employee Retirement System (ERS)
 - Judicial Retirement System (JRS)
 - Teacher Retirement System (TRS)
 - Additional (Electronic) Lottery
 - Unemployment Insurance Fund
 - Corp for the Industries of Blind, Mentally Retarded, and Other Disabled People of Puerto Rico
 - Puerto Rico Municipal Finance Corporation
 - Maritime Shipping Authority
 - Special Communities Perpetual Trust
 - Traditional Lottery

EXHIBIT 36: LIST OF ENTITIES EXCLUDED FROM THE 2021 FISCAL PLAN

Entities issuing a standalone fiscal plan

- Governmental Development Bank of Puerto Rico
- Puerto Rico Aqueduct and Sewer Authority
- Municipal Revenues Collection Center (CRIM)
- Puerto Rico Electric Power Authority
- Puerto Rico Highways and Transportation Authority ^[1]
- Puerto Rico Industrial Development Company
- Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives
- University of Puerto Rico ^[2]

Entities excluded from fiscal plan

- Agency Fund (Special Deposit Fund)
- Public Finance Corporation
- Commonwealth of Puerto Rico Regional Center Corporation
- Puerto Rico Government Investment Trust Fund
- Puerto Rico Municipal Finance Agency
- Puerto Rico Municipal Finance Corporation
- Puerto Rico Water Pollution Control Revolving Fund
- Safe Drinking Water Treatment Revolving Loan Fund
- The Children's Trust Fund
- Tourism Development Fund

[1] Commonwealth Fiscal Plan includes HTA general fund appropriations
[2] Commonwealth Fiscal Plan includes UPR general fund appropriations

Chapter 16. Macroeconomic projections

16.1 Economic and demographic trends

EXHIBIT 37: MACROECONOMIC TRENDS

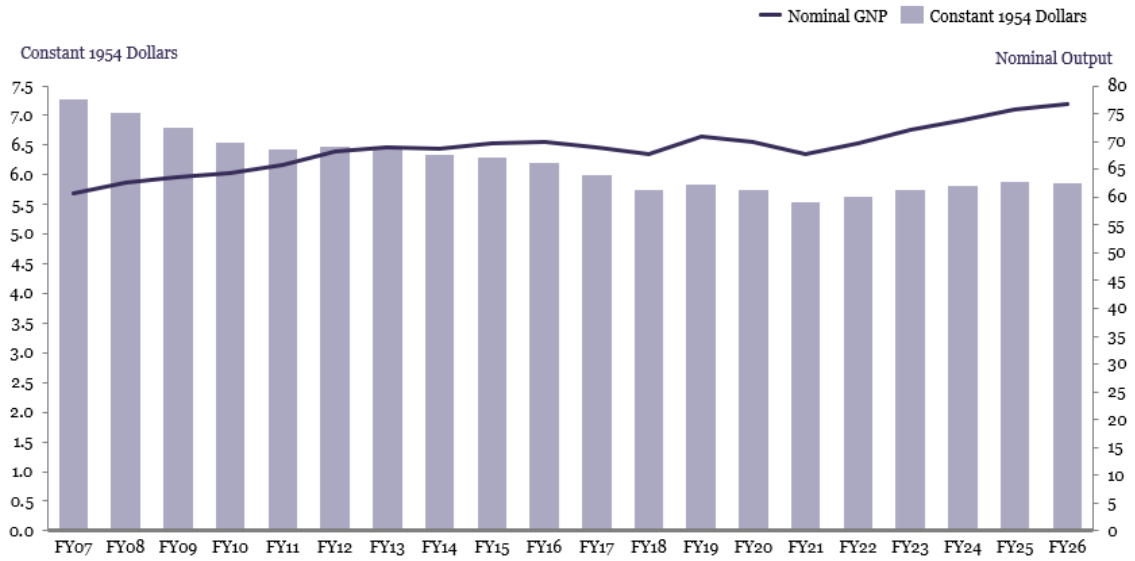


EXHIBIT 38: POPULATION TREND (M)

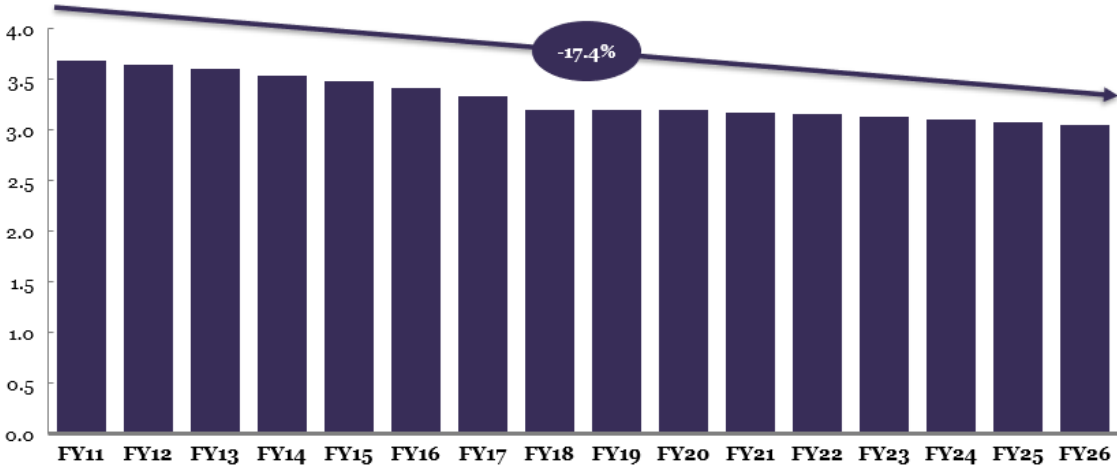
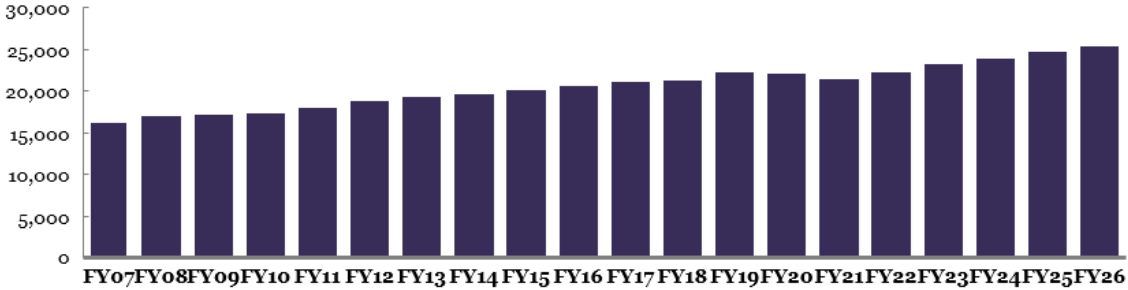


EXHIBIT 39: PER CAPITA GNP TREND (USD)



Chapter 17. Financial projections

17.1 Detailed financial projections

EXHIBIT 40: MACROECONOMIC OVERVIEW OF PUERTO RICO, FY2021-FY2026

Projections	FY2021	FY2022	FY2023	FY2024	FY2025	FY2026	FY21-26
Populations, Thousands	3,170	3,149	3,124	3,097	3,069	3,039	
Population growth rate, %	-0.45%	-0.66%	-0.80%	-0.86%	-0.92%	-0.98%	
Real GNP growth %	-3.57%	1.73%	2.06%	1.00%	1.08%	-0.32%	
Nominal GNP, \$M	67,800	69,729	72,114	73,871	75,747	76,612	
Nominal GNP per capita, \$	21,387	22,141	23,082	23,850	24,682	25,210	
Nominal GNP, per capita growth %	-2.4%	3.5%	4.2%	3.3%	3.5%	2.1%	
Inflation, %	0.71%	1.10%	1.33%	1.42%	1.44%	1.47%	
Disaster funding, \$M	7,202	11,976	8,608	7,150	8,128	4,359	47,423
Revenues, \$M	24,701	25,366	25,659	26,239	26,810	27,253	156,029
Commonwealth Revenues	15,804	14,554	14,446	14,707	14,975	15,106	89,592
Federal transfers	8,897	10,812	11,213	11,532	11,836	12,147	66,437
Expenditures, \$M	(23,084)	(24,302)	(24,816)	(25,058)	(25,497)	(25,712)	(148,469)
Commonwealth-funded expenditure	(13,330)	(12,584)	(12,672)	(12,581)	(12,703)	(12,593)	(76,462)
Federally-funded expenditures	(8,897)	(10,812)	(11,213)	(11,532)	(11,836)	(12,147)	(66,437)
Other Expenditures Outside of Budget	(858)	(906)	(931)	(945)	(958)	(972)	(5,570)
Gap / Surplus, \$M	1,617	1,065	843	1,182	1,313	1,541	7,560
Contractual debt service payments	-	(790)	(771)	(752)	(625)	(604)	(3,543)
Net gap / surplus, \$M	1,617	274	71	430	688	937	4,018

EXHIBIT 41: REVENUE BREAKDOWN

Fiscal Year Ending June 30, \$M	FY2021	FY2022	FY2023	FY2024	FY2025	FY2026	FY21-26
General Fund Revenues:							
Individual Income Taxes	2,147	1,702	1,657	1,697	1,738	1,758	10,698
Corporate Income Taxes	2,152	1,699	1,623	1,662	1,701	1,722	10,559
Non-Resident Withholdings	405	366	351	356	363	365	2,206
SUT Collections (General Fund)	2,133	2,144	2,213	2,259	2,308	2,319	13,375
Act 154 Collections	1,602	1,447	1,199	1,199	1,199	1,199	7,846
Alcoholic Beverages	277	278	280	281	283	284	1,684
Cigarettes	98	99	100	101	102	102	601
Motor Vehicles	471	408	419	425	432	433	2,588
Excises on Off-Shore Shipment Rum	238	217	197	198	199	200	1,249
Other General Fund Revenue	940	824	852	873	895	905	5,289
Sub-Total, General Fund Revenues	10,462	9,186	8,890	9,052	9,219	9,288	56,097
Other Revenues:							
Other Tax Revenues	2,074	2,063	2,070	2,096	2,122	2,137	12,562
Component Unit Revenue	1,053	1,092	1,211	1,237	1,262	1,277	7,133
SRF Revenue for CW Agencies	1,786	1,773	1,816	1,848	1,879	1,896	10,999
Third party ASES Receipts	309	320	333	347	361	376	2,046
Additional SUT (FAM & CINE)	120	121	125	128	131	132	756
Sub-Total, Other Revenues	5,342	5,369	5,556	5,655	5,756	5,818	33,495
Total, Own Source Revenues	15,804	14,554	14,446	14,707	14,975	15,106	89,592
Federal Transfers:							
Fed Transfers - Central Gov't (Exc. Medicaid)	5,728	5,829	5,906	5,990	6,077	6,166	35,696
Fed Transfers - to IFCU's (Exc. Medicaid)	327	226	237	240	243	246	1,519
Fed Transfers - Medicaid	2,842	4,757	5,069	5,302	5,516	5,735	29,222
Sub-Total, Federal Transfers	8,897	10,812	11,213	11,532	11,836	12,147	66,437
Total, Revenues	24,701	25,366	25,659	26,239	26,810	27,253	156,029

EXHIBIT 42: SUMMARY OF EXPENDITURES

Fiscal Year Ending June 30, \$M	FY2021	FY2022	FY2023	FY2024	FY2025	FY2026	FY21-26
General Fund Expenses:							
Payroll Expense	(2,875)	(2,746)	(2,721)	(2,754)	(2,789)	(2,824)	(16,709)
Operating Expense	(1,293)	(1,205)	(1,194)	(1,205)	(1,216)	(1,228)	(7,342)
Pension Expense	(2,055)	(2,114)	(2,055)	(2,055)	(2,049)	(2,043)	(12,370)
Capital Expenditures	(332)	(316)	(322)	(327)	(332)	(337)	(1,966)
Medicaid Expense	(316)	(470)	(566)	(590)	(611)	(635)	(3,188)
Appropriations	(973)	(983)	(943)	(878)	(877)	(838)	(5,493)
Other Misc. Items - Recurring	(963)	(1,041)	(1,210)	(1,143)	(1,176)	(1,022)	(6,555)
Other Misc. Items - Non-Recurring	(1,237)	(458)	(349)	(257)	(219)	(188)	(2,708)
Sub-Total, General Fund Expenses	(10,045)	(9,333)	(9,362)	(9,209)	(9,269)	(9,113)	(56,331)
Special Revenue Fund Expenses:							
Component Units	(1,190)	(1,158)	(1,167)	(1,185)	(1,202)	(1,218)	(7,120)
CW Agencies	(1,786)	(1,773)	(1,810)	(1,840)	(1,870)	(1,886)	(10,965)
Medicaid	(309)	(320)	(333)	(347)	(361)	(376)	(2,046)
Sub-Total, Special SRF Expenses	(3,284)	(3,251)	(3,310)	(3,372)	(3,434)	(3,479)	(20,131)
Federal Fund Expenses:							
FF - Central Gov't (Exc. Medicaid)	(5,728)	(5,829)	(5,906)	(5,990)	(6,077)	(6,166)	(35,696)
FF - to IFCU's (Exc. Medicaid)	(327)	(226)	(237)	(240)	(243)	(246)	(1,519)
FF - Medicaid	(2,842)	(4,757)	(5,069)	(5,302)	(5,516)	(5,735)	(29,222)
Sub-Total, Federal Fund Expenses	(8,897)	(10,812)	(11,213)	(11,532)	(11,836)	(12,147)	(66,437)
Other Expenditures Outside of Budget	(858)	(906)	(931)	(945)	(958)	(972)	(5,570)
Total, Expenses	(23,084)	(24,302)	(24,816)	(25,058)	(25,497)	(25,712)	(148,469)
Surplus/(Deficit) - Excl. Debt Payments	1,617	1,065	843	1,182	1,313	1,541	7,560
Debt Service	-	(790)	(771)	(752)	(625)	(604)	(3,543)
Surplus/(Deficit) - Incl. Debt Payments	1,617	274	71	430	688	937	4,018

EXHIBIT 43: AGENCY GROUPINGS

Agriculture	Agricultural Enterprises Development Administration	Puerto Rico Department of Agriculture
	Agricultural Insurance Corporation	
Economic Development	Department of Economic Development & Commerce	Puerto Rico Tourism Company
	Office of Industrial Tax Exemption	Puerto Rico Trade & Export Company
	Permits Management Office	Redevelopment Authority of Roosevelt Roads
	Puerto Rico Planning Board	State Office of Energy Policy
Environmental	Puerto Rico Regional Center Corporation	
	Department of Natural and Environmental Resources	Puerto Rico Environmental Quality Board
State	Natural Resources Administration	Solid Waste Authority
	Puerto Rico Council on Education	Puerto Rico Department of State
Public Safety	9-1-1 Emergency Systems Bureau	Puerto Rico Department of Public Safety
	Emergency and Disaster Management Bureau	Puerto Rico Fire Department Bureau
	Forensic Science Bureau	Puerto Rico Police Bureau
	Medical Emergency Corps Bureau	Special Investigations Bureau
Utilities Commission	Energy Commission	Public Service Regulatory Board
	Independent Office for Consumer Protection	Telecommunications Regulatory Board
	Public Service Commission	