Working Group for the Fiscal and Economic Recovery of Puerto Rico

Puerto Rico Fiscal and Economic Growth Plan

Prepared by the Working Group for the Fiscal and Economic Recovery of Puerto Rico Pursuant to Executive Order 2015-022

September 9, 2015

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Executive Summary

Executive Summary

This document contains the key findings of the Working Group for the Fiscal and Economic Recovery of Puerto Rico (the "Working Group") established by Governor Alejandro García Padilla by executive order (EO 2015-022), and the measures recommended by the Working Group to reduce the Commonwealth's projected financing gaps. Such measures comprise the "Fiscal and Economic Growth Plan" or "FEGP".

- Despite the significant historical measures undertaken by the Commonwealth since the onset of the financial crisis in 2007 to reduce expenses, increase revenues and address structural challenges, the Working Group projects that, absent meaningful additional fiscal and structural reforms, the consolidated government will incur significant financing gaps for at least the next five years
  - The cumulative financing gap for the Commonwealth is projected to be $27.8 billion from fiscal year ("FY") 2016 to FY 2020 absent corrective action
  - In addition, the Puerto Rico Treasury's single cash account (the "TSA"[1]) and the Government Development Bank for Puerto Rico (the "GDB") are each expected to exhaust their liquidity before the end of calendar year 2015
- In connection with this fiscal and economic emergency, the Working Group and its advisors examined the various causes of the fiscal and economic challenges facing the Commonwealth, and potential reform measures to address these challenges
- Following this review, the Working Group developed the FEGP, setting forth economic development, structural, fiscal and institutional reform measures intended to meaningfully reduce the Commonwealth's projected financing gaps
  - The Working Group believes that the Commonwealth could reduce its cumulative financing gap by over $11.9 billion from FY 2016 to FY 2020, through a combination of revenue increases and expense reductions[2]
    - Economic growth, if achieved, could reduce the cumulative financing gap another $1.9 billion

(1) The TSA account is the account through which General Fund's (as that term is used in the Commonwealth's comprehensive annual financial reports) expenses flow as well as certain other governmental funds. It excludes GDB balances and public corporations such as HTA (though certain tax revenues collected by the Commonwealth before transfer to a public corporation do flow through the TSA).
(2) Net of assumed incremental costs associated with these measures.

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- In order to ensure compliance with the FEGP measures, the Working Group proposes the implementation of a control board and new budgetary regulations, pursuant to proposed legislation known as the Fiscal Responsibility and Economic Revitalization Act ("FRERA")
- In addition to the local policy reforms, the Working Group believes that meaningful changes to US federal policies are critical to the ability of the Commonwealth to meet its debt service costs while providing funding for essential services to its residents, most particularly changes in the areas of health care funding and tax policies for economic development. Moreover, the Working Group believes Puerto Rico must have an orderly process to restructure its liabilities
- Even after the implementation of the FEGP, which is subject to significant political and execution risks, the Working Group's projections suggest that the Commonwealth cannot meet all of its debt service requirements as currently scheduled and must restructure its liabilities
  - After accounting for the estimated impact of all measures *and* including the benefit of potential economic growth spurred by structural reforms, the Working Group still projects the Commonwealth to have a cumulative financing gap from FY 2016 to FY 2020 of $14 billion
- While the Working Group recognizes that a restructuring of the Commonwealth's debt would result in hardship to individual bondholders, unless the persistent stagnation of Puerto Rico's economy that has helped fuel the increase in Government debt over the past decade can be reversed, the public debt is not sustainable
  - Further, paying debt service as currently scheduled in the face of significant financing gaps could severely impair the Commonwealth's ability to provide essential services to its residents

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- As difficult as debt restructuring is likely to be (particularly in the absence of an effective federal or Commonwealth public debt restructuring legal framework), the Working Group recommends that the Commonwealth advisors begin work on a voluntary exchange offer to be made to its creditors as part of the implementation of the FEGP
  - The Working Group has directed the Commonwealth's advisors to take into account the priority accorded to various debt instruments across the Puerto Rico debt complex while recognizing that, even assuming the clawback of revenues supporting certain Commonwealth tax supported debt, available resources may be insufficient to service all principal and interest on debt that has a constitutional priority
  - Therefore, a consensual compromise of the creditors' competing claims to the Commonwealth's revenues to support debt service will be required in order to avoid a disorderly default on the Commonwealth's debt and a legal morass that will further destabilize the Commonwealth's economy and finances
- Accordingly, the Working Group recommends that the Commonwealth advisors meet with the creditor groups that have already been organized (and those that may be formed hereafter) to explain the Fiscal and Economic Growth Plan and to begin negotiation of the terms of a voluntary exchange offer that can garner widespread creditor acceptance
- **It is the Working Group's belief that a voluntary adjustment of the terms of the Commonwealth's debt that allows the measures contained in the FEGP to be implemented is the best way to maximize all creditor recoveries**

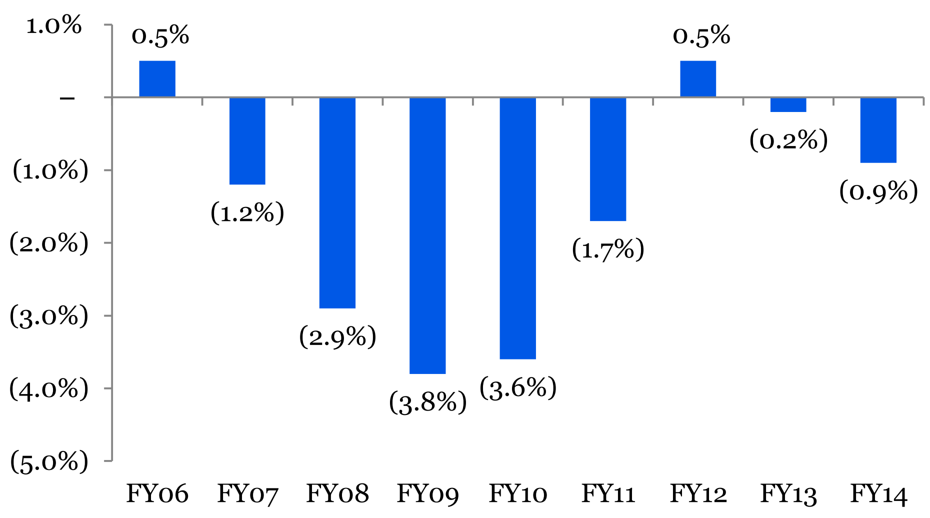
Historical Reform Measures and Current Liquidity and Fiscal Position

Economic Decline of Puerto Rico

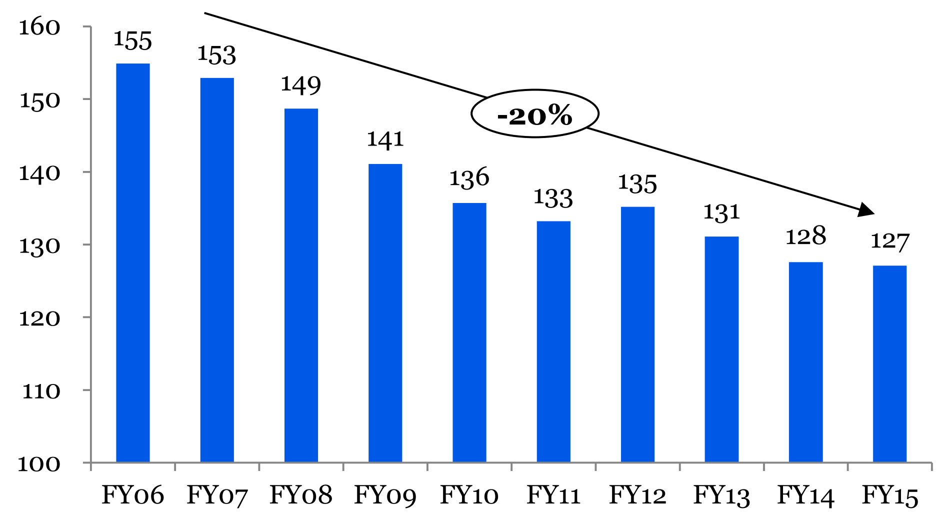
Since the expiration of Section 936 of the US Internal Revenue Code in 2006[(1)] and the onset of the global financial crisis in 2007, the Commonwealth has faced virtually continuous economic decline, in spite of substantial stimulus spending

- GNP growth has been negative nearly every year since FY 2007; little growth was recorded in the prior decade
- The lower rate of GNP decline since FY 2009 is due in large part to the large amount of stimulus and deficit spending injected into Puerto Rico's economy during the same period
  - For example, the Commonwealth was allocated approximately $7.1 billion of funds through the American Recovery and Reinvestment Act ("ARRA") and, using the Puerto Rico Sales Tax Financing Corporation ("COFINA") bond proceeds from offerings in 2009 and 2010, the Commonwealth created a $500 million "Local Stimulus Fund"
  - Furthermore, tax reform enacted in 2011 sought to jumpstart the economy by reducing individual and corporate taxes by approximately $706 million, some of the provisions of which were later modified to deal with resulting revenue shortfalls

Real GNP Growth[(2)]



GDB EAI Index[(2)(3)]



(1) Insofar as is relevant to Puerto Rico, Section 936 of the US Internal Revenue Code exempted from US taxation certain income derived by US companies from the active conduct of a trade or business in Puerto Rico and certain Puerto Rico sourced investment income.
(2) Source: Economic Activity Index ("GDB – EAI") report for June 2015.
(3) Values are as of June 30 of each year. The apex in FY 2006 occurred at 158.0 in July. EAI is comprised of four indicators: total payroll employment; total electric power generation; cement sales and gas consumption. The index is highly correlated to Puerto Rico's real GNP. For additional details on the EAI, see the GDB website under "Economy."

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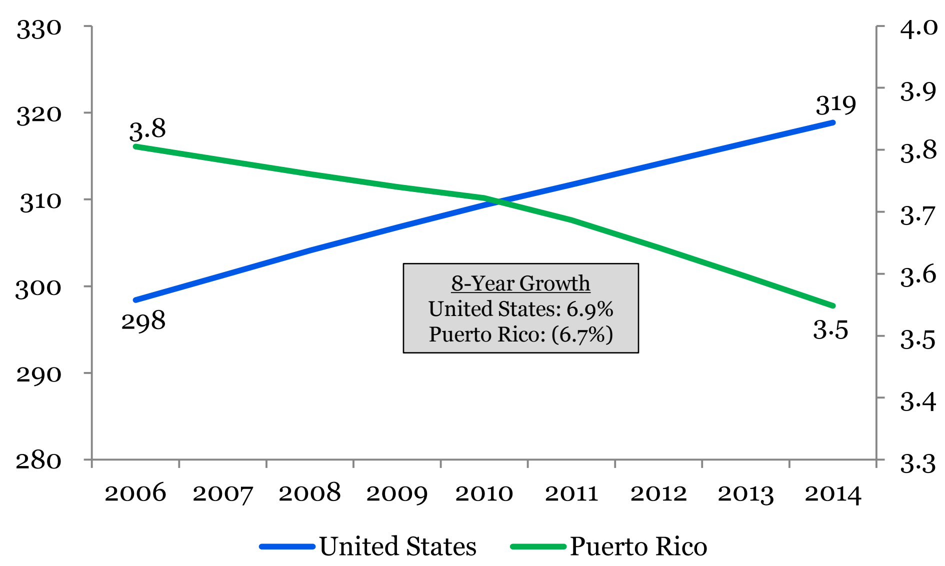
Deteriorating Economic Prospects & Demographic Trends

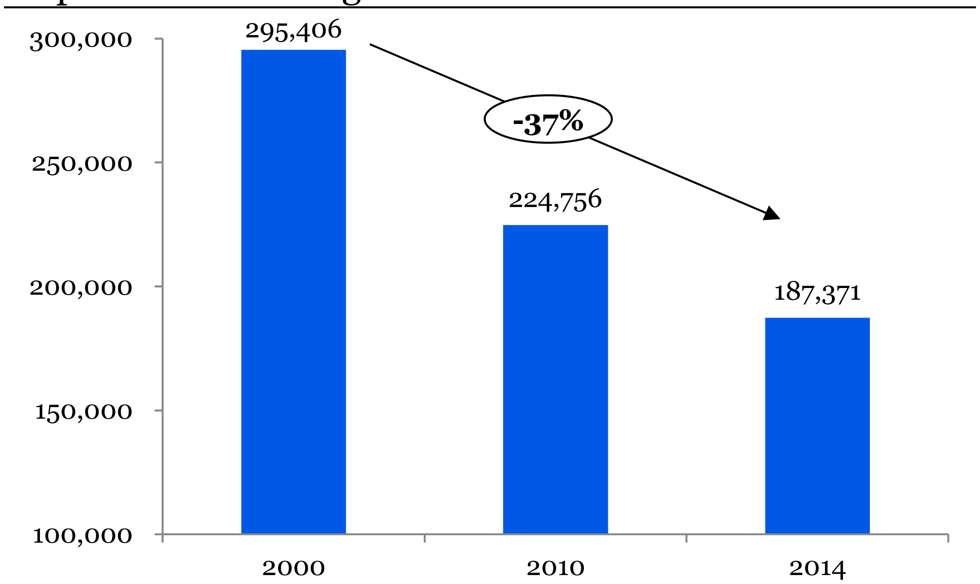
Reduced economic activity has had a marked effect on the residents of the Commonwealth, leading to stagnating incomes and increasing outmigration to the mainland

- As multinational corporations moved out of the Commonwealth following the expiration of Section 936 and without substantial job creation, cumulative per capita income growth of 5.5%[(1)] from 2006 to 2013 has failed to keep pace with cumulative inflation of ~15%[(2)] over the same time period
- Deteriorating economic conditions have therefore led to many Puerto Ricans emigrating to the mainland
- The Commonwealth averaged net outmigration of approximately 48,000 residents per year from 2010 to 2013[(3)], with 42% of emigrants stating that their primary reason for moving was job-related; in 2013, approximately 74,000 residents emigrated to the mainland[(4)]
- The remaining population is also becoming increasingly elderly and outside the labor force
  - Persons 60 years and older represent more than 20% of the population (the highest in the United States) and their labor participation rates range from 10.7% to 13.3%[(5)]; children aged five years or less have decreased from 295,406 in 2000 to approximately 187,371 in 2014, a reduction of 37%[(6)]

Population Data (millions)[(6)]



Population Under Age Five[(6)]



(1) Per capita income from World Bank. 2013 is the most recent year for which data is available for both Puerto Rico and the US.
(2) Inflation calculated using CPI as presented by GDB and sourced to Dept. of Labor and Human Resources.
(3) Puerto Rican Population Declines on Island, Grows on US Mainland, Pew Research Center, August 11, 2014.
(4) Puerto Rico Statistics Institute, “Perfil del Migrante 2013”, February 8, 2015.
(5) Puerto Rico Planning Board, “Resumen Economico de Puerto Rico”, December 2013.
(6) US Census Bureau.

Significant Fiscal Responsibility Measures

The Commonwealth has repeatedly taken difficult measures to reduce its consolidated financing gaps

- The following chart represents a select subset of the various measures that the Commonwealth has taken since the onset of the economic crisis

Revenues	Expenditures	Other Fiscal Responsibility Measures
2007: 7% Sales and Use Tax ("SUT") implemented ~$1.1bn per year	**2010:** Voluntary resignation and work-day reduction programs ~$91mm	**2011:** Gradually increase employer contribution to ERS from 9.275% to 20.525%
2011: Act 154-2011 institutes annually declining 4% excise tax on multinationals operating in Puerto Rico ~$1.9bn per year	**2010:** Temporary suspension of certain laws, collective bargaining agreements and other contractual agreements ~$187mm	**2011:** Gradually increase employer contribution to TRS from 8.5% to 19.75% per employee
2011: UPR[(1)] stabilization fee ~$40mm per year (later repealed)	**2011:** Involuntary layoffs ~$367mm	**2011:** Complete public-private partnership ("P3") of PR-22
2013: Act 154 excise tax reset at 4% rate	**2013:** Eliminate subsidies to PRASA[(2)] (due to PRASA rate increase) ~$340mm	**2013:** Complete P3 of LMM International Airport
2013: Petroleum products tax increase from $3.00 to $9.25 per barrel ~$190mm per year	**2014:** Reduction in non-salary benefits ~$51mm (prohibited December bonus above $600 and liquidations of unused vacation or sick leave); government merit bonuses eliminated	**2013:** Increase employee contribution to ERS[(3)] from 8% to 10%; eliminate special law benefits to ERS retirees; increase retirement age
2014: Gross profits tax on corporations ~$300mm per year	**2014:** Judicial and legislative budget reductions ~$45mm	**2013:** Increase employee contribution to TRS[(4)] from 9% to ~13%; eliminate special law benefits to TRS retirees; increase retirement age (ruled unconstitutional in part)
2014: SUT charged at point of entry ~$70mm per year	**2014:** UPR, Judicial and Municipality appropriation levels frozen from 2015-2017; CBA salary increases frozen	**2013:** Eliminate "scoop and toss"[(5)] of PBA[(6)] debt service ($175mm in FY 2013)
2015: Petroleum products tax raised from $9.25 to $15.50 per barrel, providing an incremental ~$170mm per year	**2015:** School transportation cost reductions and school consolidations ~$110mm	**2014:** Eliminate "scoop and toss"[(5)] of GO[(7)] debt service ($575mm in FY 2014)
2016: SUT increased from 7% to 11.5% and VAT[(8)] instituted; projected ~$1.1-$1.3bn per year	**2013-2015:** 3% annual payroll reduction	**2014:** Prohibit deficit financings by GDB

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(1) University of Puerto Rico ("UPR").
(2) Puerto Rico Aqueduct and Sewer Authority ("PRASA").
(3) Employees Retirement System ("ERS").
(4) Teachers Retirement System ("TRS").
(5) "Scoop and Toss" generally refers to the elimination of annual debt principal and interest through a refinancing with delayed payment dates.
(6) Public Buildings Authority ("PBA").
(7) General Obligation ("GO").
(8) Value Added Tax ("VAT").

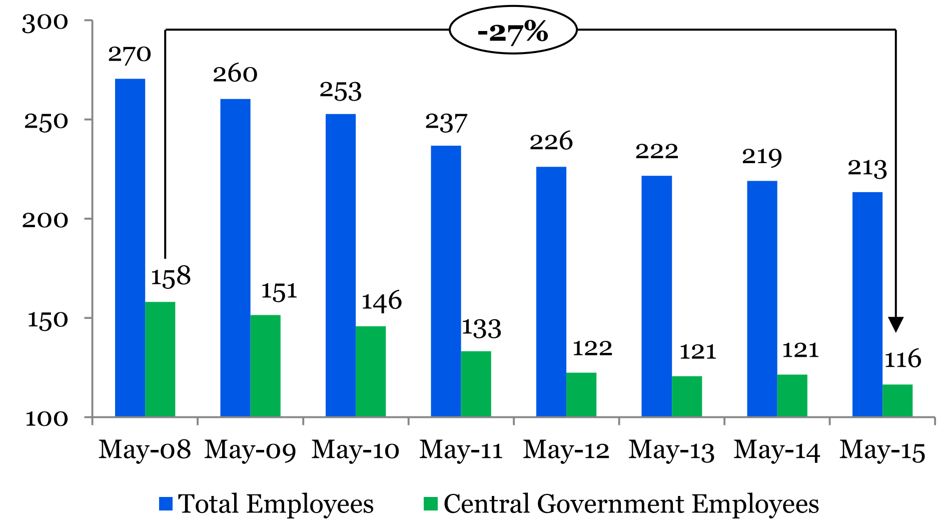
Select Results of Historical Measures to Date

As a result of the Commonwealth's expense reduction measures, central government employee headcount is down 27% (4.3% compounded annual decline) since 2008; further, revenue measures have allowed projected General Fund revenues for FY 2016 to grow by 23% since a recession low in FY 2009

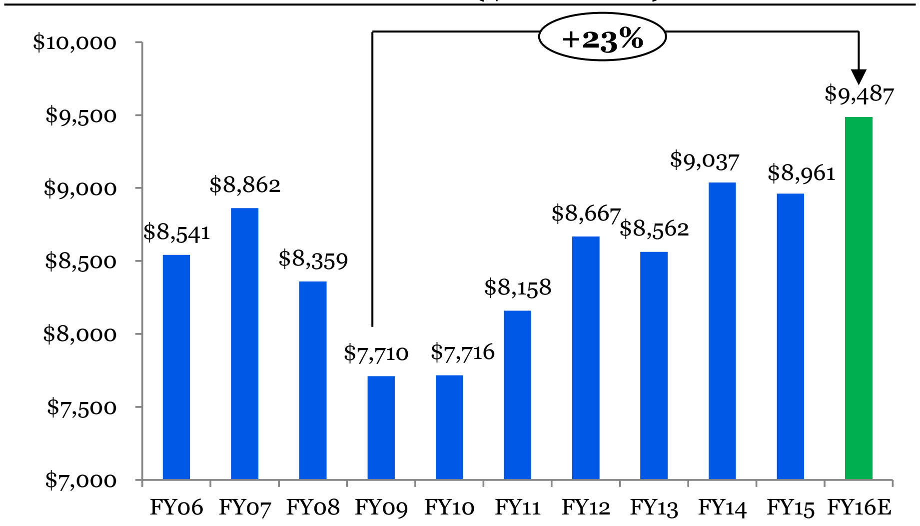
- Note that the General Fund revenue numbers shown below do not account for the incremental revenues that were also added at PRASA (through a rate increase), Puerto Rico Highways and Transportation Authority ("HTA") (through increased petroleum products taxes), Puerto Rico Infrastructure Financing Authority ("PRIFA") (also through petroleum products taxes) and other entities on the island which received governmental subsidies from the General Fund or GDB

- According to US Government Accountability Office, in 2012 government employment as a share of the population was 8.7% in Puerto Rico vs. 8.9% in the states[1]. Since 2012 there has been a further reduction of approximately 13,000 in the number of Puerto Rican government employees through attrition

Government Employee Headcount Reduction[2] (thousands)



General Fund Revenues[3][4] ($ millions)



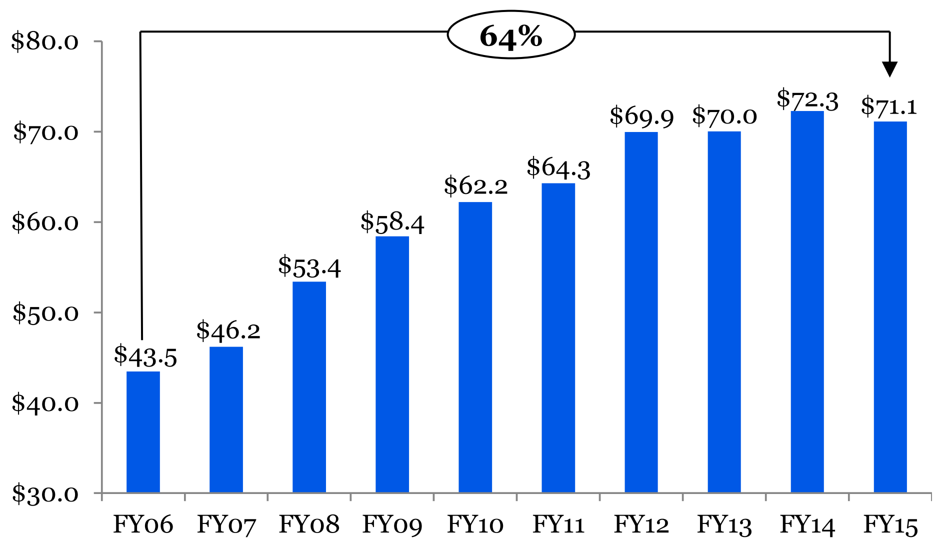
(1) US Government Accountability Office, Information on How Statehood would Potentially Affect Selected Federal Programs and Revenue Sources, March 2014.
(2) Source: Puerto Rico Statistics Institute, May 2015 Employment Report. Central government employees include Office of the Governor, Departments and Agencies, Judicial Branch and Legislative Branch as described in the report.
(3) Source: Puerto Rico Treasury website. Note that the numbers shown correspond to "Total Revenues" and not "Total Budgetary Revenues." See page 100 of the Commonwealth's Financial Information and Operating Data Report from October 30, 2014 for a historical reconciliation of "Total Revenues" to "Total Budgetary Revenues."
(4) FY 2016 General Fund revenue represents projections based on the work of Conway MacKenzie ("CM") and is inclusive of incremental SUT/VAT taxes projected to be collected on account of tax reform.

Debt Accumulation

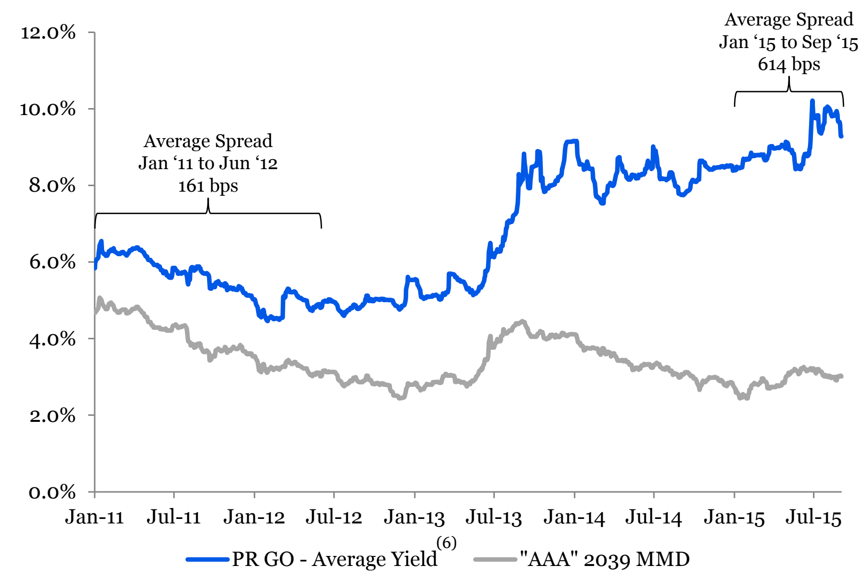
Notwithstanding the Commonwealth's liquidity-enhancing measures, total debt has grown by approximately 64% since FY 2006

- This rising debt burden has increased total debt financing costs and has resulted in an increasing percentage of the budget being redirected from investment and essential services to debt service
- Increased financing costs are reflected in the rising yields of Puerto Rico GO bonds as compared to similar municipal bonds
  - Whereas in 2006, GO bonds with 20 years to maturity were priced to yield 4.8%, the March 2014 GOs due in 2035 (approximately 20 years to maturity) were issued to yield 8.7% and currently yield 11.3%[1]
- Given these yields, market access on sustainable terms is not currently available to the Commonwealth

Historical Public Sector Debt[2][3][4] ($ billions)



Puerto Rico GO Yields vs. 2039 MMD[5]



(1) Yield on 2006 issuance from Public Improvement Bonds of 2006, Series A Offering Statement and 2014 GO current yield from Bloomberg.
(2) For more detail see the appendix for total public sector debt as of June 30, 2015. Data per GDB.
(3) Balances shown do not include the accreted value of capital appreciation bonds ("CABs"). As of July 1, 2015, the incremental accreted value of the CABs was $2.6 billion, with another $31.3 billion of accretion remaining.
(4) Does not include unfunded pension liabilities. Based on preliminary valuation reports as of June 30, 2014, the Employees Retirement System, Teachers Retirement System and Judiciary Retirement System ("JRS") net pension liabilities were $30 billion, $13 billion and $442 million, respectively. See the May 7, 2015 Commonwealth of Puerto Rico Quarterly Report for more details.
(5) Puerto Rico GO bond valuation from Standard & Poor's (J.J. Kenny Evaluated Pricing Service). "AAA" MMD based on 2039 maturity, which was chosen as the benchmark as it is within the maturity range of the uninsured PR GO bonds included.
(6) Simple average of the historical Standard & Poor's (J.J. Kenny Evaluated Pricing Service) valuations for seven long-duration, tax-exempt, uninsured, current interest PR GO Bonds (CUSIPs: 74514LB71, 74514LB89, 74514LE86, 74514LWA1, 74514LKE6, 74514LXH5, 74514LYW1).

Extraordinary Liquidity Measures Taken in FY 2016

Despite historical attempts to strengthen the Commonwealth's liquidity, the TSA account would have exhausted its liquidity had certain extraordinary liquidity measures not been taken for FY 2016, including:

- Funding $400 million of its working capital needs through emergency "intra-governmental" loans funded by requiring its proprietary insurance companies to liquidate their securities portfolios(1);
- Withholding GO set asides totaling approximately $93 million per month;
- Requiring its insolvent pension systems to pre-fund benefit payments to retirees, which improved cash flow by approximately $295.0 million in July 2015 and an expected $141.0 million in each of October 2015, December 2015 and February 2016;
- Having GDB refinance the 2015 C-Series tax revenue anticipation notes ("TRANs") ($300 million) in July 2015, notwithstanding GDB's fragile liquidity position; and
- Delaying payment of approximately $291.0 million in income tax refunds from the 2014 tax year
  - These refunds will not be paid in full until February 2016, at the earliest

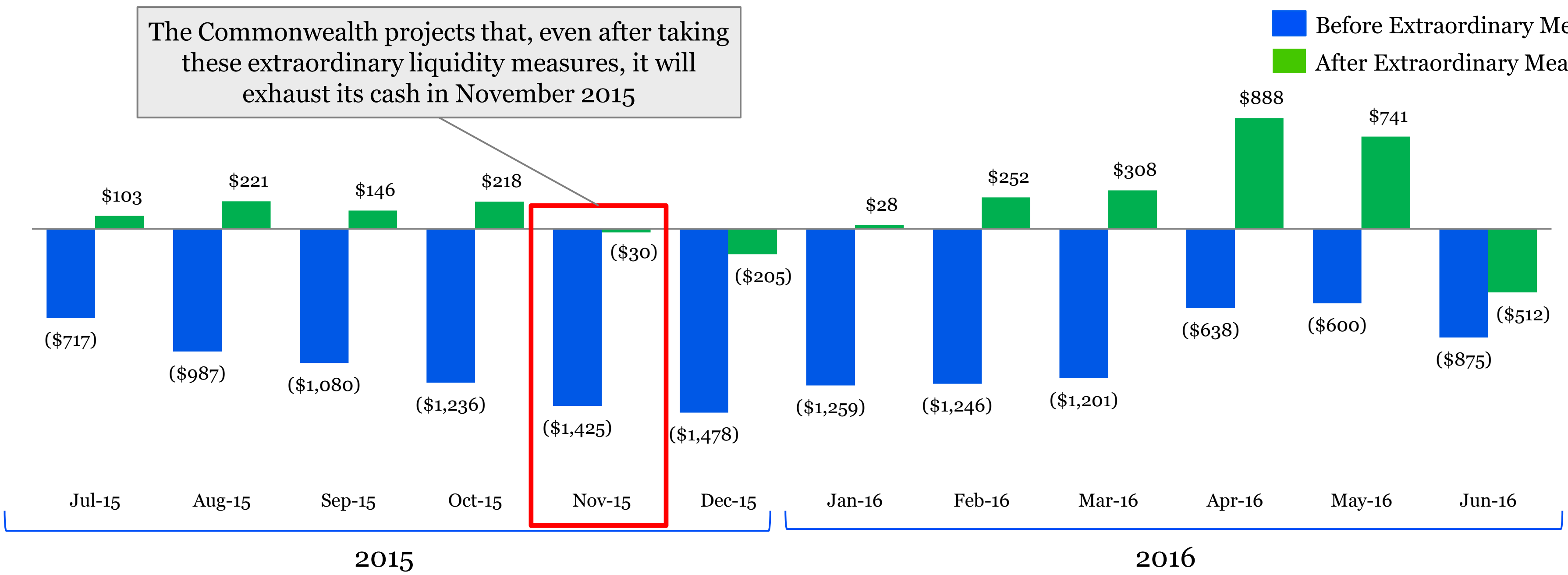
- Moreover, the measures described on the following page do not account for any shortening of outstanding days payable to third parties that today exceed $1.6 billion at Commonwealth agencies (excludes amounts owed by public corporations and agencies with independent treasuries)(2)
- **These extraordinary liquidity measures cannot be maintained on a long-term basis**

(1) Proprietary insurance companies include State Insurance Fund ("SIF"), Automobile Accidents Compensation Administration ("ACAA") and Temporary Non-Occupational Incapacity Insurance ("SINOT").
(2) Based on preliminary estimates subject to material revision; moreover, may not account for all payables as there is typically a substantial lag between the incurrence of an expense and that expense being recorded.

Projected Near-Term TSA Liquidity

Absent the Commonwealth's extraordinary and unsustainable liquidity measures described on the previous page, the TSA would have already exhausted its cash

Projected TSA Liquidity – Ending Cash Balance [1][2] ($ millions)



- GDB cannot be a source of liquidity for the Commonwealth or the public corporations
  - As of May 31, 2015, GDB had $778 million of total net liquidity, which is before any reduction for GDB's minimum liquidity requirement
  - During FY 2016, GDB has $876 million of maturing notes, $267 million of which are GO guaranteed (the payment of which is not included in the TSA projections above), and $188 million of interest due

(1) Defined in the August 25, 2015 report Commonwealth of Puerto Rico: Conway MacKenzie Liquidity Update as cash in the bank and does not reflect outstanding checks, which may represent a substantial amount.
(2) Projections do not assume any working capital impact from a reduction in days payable outstanding to trade creditors or a catch-up in the payment of overdue tax refunds.

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Overview of Commonwealth Projected Financing Gaps

Building on the work done in the report *Puerto Rico – A Way Forward*, updated as of July 13, 2015 (the "Krueger Report"), the Working Group developed a revised view of the future Commonwealth financing gaps (the revised view constituting the "Adjusted Estimates")

- As explained in the Krueger Report, which was authored by a team of former International Monetary Fund economists headed by Anne Krueger, the General Fund alone (which is the primary account associated with the TSA presented on the previous page) does not adequately capture the total financing needs of the Commonwealth
- The Working Group adopted the comprehensive approach outlined in the Krueger Report, along with many of the same key assumptions, such as an assumed baseline for real economic growth of negative 1%
- While the general approach to the financing gap projections is the same as in the Krueger Report, the Working Group conducted its own diligence and refined certain estimates based in large part on information that was not available at the time the Krueger Report was prepared
- These updates include:
  - Updated revenue projections that incorporate preliminary actual results from 2015
  - Updated component unit projections based on detailed work undertaken by the Working Group and its advisors (the Krueger Report did not have detailed individual unit projections)
  - Revised estimates of budgeted expenses and the resultant impact of Act 66
  - Revised capital expenditure estimates

Overview of Commonwealth Projected Financing Gaps

- In addition to these updates, the Adjusted Estimates include two changes to the approach taken in the Krueger Report:
  - HTA is now included in the projections, due to its reliance on taxes collected by the Commonwealth and the Commonwealth's support of HTA historically through the assignment of new revenue sources and the provision of over $2 billion of loans from GDB
  - Rather than showing estimates of retirement system shortfalls once they were projected to take place, the FEGP assumes the Commonwealth makes the additional uniform contribution (the "AUC") required by Act 3-2013 and Act 160-2013 to prevent full asset depletion. Both the Krueger Report and the Adjusted Estimates show the financing gap effectively assuming no interruption of current benefits(1)
- Additional details on the variances of the Adjusted Estimates to the Krueger Report are available in the appendix

(1) See the appendix for additional details on assumed asset balances in the retirement systems.

Projected Financing Gaps Based on Adjusted Estimates

The Working Group's revised projections indicate that the Commonwealth as a whole will face significant financing gaps for at least the next five years, absent additional measures

Central Government Outlook ($ millions)	**2016P**	**2017P**	**2018P**	**2019P**	**2020P**	**Total**
Revenues						
General Fund and Other Select Revenues[1]	$8,503	$8,519	$8,561	$8,604	$8,648	$42,835
GDB Net Operating Revenue[2]	(96)	(21)	248	307	269	706
COFINA[3]	696	724	753	783	815	3,771
Federal Transfers[4]	6,477	6,540	6,604	6,669	6,734	33,025
HTA Revenues[5]	677	636	643	645	648	3,249
Total Revenue	**16,257**	**16,399**	**16,809**	**17,009**	**17,114**	**83,587**
Noninterest Expenditure						
General Fund Budget (ex. Debt Service and Additional Uniform Contributions)[6]	(7,957)	(8,251)	(8,697)	(9,236)	(9,614)	(43,756)
Additional Uniform Contribution and Catch-up[7]	(314)	(299)	(300)	(797)	(798)	(2,509)
Net Operating Deficit of Non-General Fund Governmental Funds[8]	(235)	(237)	(240)	(242)	(244)	(1,199)
Net Operating Deficit (Surplus) of Component Units (ex. Capex and ACA Loss Impacts)[9]	(120)	59	(101)	192	324	354
Capital Expenditures[10]	(386)	(585)	(545)	(503)	(338)	(2,358)
Federal Programs[11]	(6,477)	(6,540)	(6,604)	(6,669)	(6,734)	(33,025)
HTA Expenditures (ex. Debt Service and Capex)[12]	(279)	(189)	(149)	(150)	(151)	(918)
Total Noninterest Expenditure	**(15,769)**	**(16,044)**	**(16,636)**	**(17,405)**	**(17,556)**	**(83,410)**
Additional Expenses Based on Current Policies						
Loss of Affordable Care Act ("ACA") Funding[13]	–	–	(526)	(1,597)	(1,730)	(3,853)
Act 154 / Foreign Company Tax Losses[14]	–	–	(538)	(1,075)	(1,075)	(2,688)
Total Additional Expenses Based on Current Policies	**–**	**–**	**(1,064)**	**(2,672)**	**(2,805)**	**(6,541)**
Debt Service						
Consolidated Interest[15]	(2,320)	(2,370)	(2,320)	(2,239)	(2,170)	(11,419)
Consolidated Principal[15]	(1,810)	(1,044)	(957)	(1,628)	(1,299)	(6,738)
Total Debt Service	**(4,130)**	**(3,415)**	**(3,277)**	**(3,867)**	**(3,469)**	**(18,157)**
Identified Financing Sources (Uses)						
Change in Stock of Payables[16]	–	(827)	(501)	(501)	(501)	(2,331)
Net Deposit Draw/(Replenishment)[17]	(538)	(500)	–	–	–	(1,038)
Inflows from Other Entities[18]	105	–	–	–	–	105
Identified Financing Sources (Uses)	**(433)**	**(1,327)**	**(501)**	**(501)**	**(501)**	**(3,264)**
Total Estimated Financing Gap before Measures	**($4,075)**	**($4,386)**	**($4,670)**	**($7,437)**	**($7,217)**	**($27,786)**
Memo: Debt Service as a % of Total Revenue ex. Federal Transfers[19]	*42%*	*35%*	*32%*	*37%*	*33%*	*36%*

Note: Revenues do not include any incremental tax revenues attributable to the increased SUT or transition to the VAT which would reduce the projected financing gap by $6.350 billion (See page 56). For footnotes and additional details on the projections included herein, please see the appendix.

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Fiscal and Economic Growth Measures

Scope & Process of the Fiscal and Economic Growth Plan

In order to address the challenges facing the Commonwealth, Governor García Padilla tasked the Working Group to develop a Fiscal and Economic Growth Plan

- The creation of the Working Group was in direct response to the Krueger Report regarding the fiscal and economic situation of the Commonwealth and the sustainability of its debt
- The Governor's executive order mandates that the Working Group evaluate the measures outlined in the Krueger Report and ultimately design a plan to address short and long-term fiscal challenges facing the Commonwealth by recommending measures to:
  - Address financing gaps and the debt load;
  - Ensure budget compliance;
  - Provide greater financial transparency; and
  - Carry out structural reforms necessary to restore economic competitiveness and growth
- The Working Group, in conjunction with its advisors, conducted due diligence on various Commonwealth funds, agencies and public corporations that are supported by taxes and appropriations and contributed to the fiscal deficits identified in the Krueger Report, in order to create a holistic projection of Commonwealth finances
- After identifying and estimating key contributors to historical and future Commonwealth-wide deficits, the Working Group also examined various measures outlined on the following pages that will help address the financing gaps identified in the Krueger Report

FEGP Measures

"The situation is acute in the face of faltering economic activity, faltering fiscal and debt sustainability, and faltering policy credibility. A comprehensive program that tackles all three has a better chance of success than a partial approach, and the advantage of sharing the costs and benefits of reform across government, workers, businesses, and creditors." –The Krueger Report p.26

1. Economic Growth and Structural Reform

1.1 Stimulate Employment and Labor Force Participation
1.2 Diversify Fuel Base and Stabilize Energy Rates
1.3 Implement Pro-Growth Corporate Tax Regime
1.4 Reduce Costs and Improve Ease of Doing Business
1.5 Invest in Strategic Infrastructure

2. Fiscal Stability

Revenue Enhancing Measures

2.1 Complete Transition to VAT
2.2 Stabilize Corporate Tax Revenue Base
2.3 Improve Tax Administration and Enforcement

Expense Reduction Measures

2.4 Reduce Operating Costs
2.5 Cut Governmental Subsidies
2.6 Right-Size Department of Education
2.7 Control Health Care Costs
2.8 Leverage P3s to Deliver Quality and Cost-Efficient Services

3. Institutional Reform and Transparency

3.1 Install New Accounting and Financial Systems
3.2 Establish Centralized Treasury Functions
3.3 Improve Fiscal and Economic Decision-Making
3.4 Implement New Budgetary Rules
3.5 Institute Control Board for Policy Continuity and Compliance

Economic Growth and Structural Reform

"Restoring growth requires restoring competitiveness. Key here is local and federal action to lower labor costs gradually and encourage employment (minimum wage, labor laws, and welfare reform), and to cut the very high cost of electricity and transportation (Jones Act). Local laws that raise input costs should be liberalized and obstacles to the ease of doing business removed." –The Krueger Report p.1

Economic Growth and Structural Measures	Target Date

1.1 Stimulate Employment and Labor Force Participation

Only 40% of Puerto Rico's adult population (vs. 63% in the US) is employed or looking for work. A significant portion of the population is either receiving welfare, informally employed or both. The Commonwealth must **adopt pro-growth labor market policies, reform welfare programs and determine policy with respect to its minimum wage**

Private Sector Labor Reform — January 2016

- Enact legislation to reform current labor laws to incentivize growth and boost labor participation
  - Establish a uniform work day and enable employers to provide flexible work week schedule
    - 8-hour work day based on calendar days, not consecutive 24 hour periods
    - Provide option for overtime to be calculated based on hours worked in excess of 40 hours per week, not in excess of 8 hours per day
  - Incentivize businesses, including small and medium enterprises ("SMEs"), to expand job opportunities
    - Ease December bonus payment waiver process
    - To incentivize youth employment and reverse emigration trends, make discretionary December bonus payment to employees 25 and under
    - Modify mandatory vacation days for all new hires based on sliding scale tiered off an employee's years of employment
    - Extend employment probation period to one year

Economic Growth and Structural Reform

Economic Growth and Structural Measures	**Target Date**

1.1 Stimulate Employment and Labor Force Participation (cont.)

- Reform mandatory severance; allow performance-based retention
  - Apply Act 80-1976 only to "non-exempt" employees
  - Limit mandatory severance pay at six months; exclude non-cash benefits from severance calculations
  - Allow businesses to retain employees based on performance in the event of a downsizing or reorganization of operations
- Simplify and make uniform other labor market regulations, including establishing a one-year uniform statute of limitations for labor claims

- Create maternal benefits fund, funded by employer premiums, to reduce incentives for discrimination and increase labor participation while maintaining current maternity benefit level — January 2016

Welfare Reform and Stimulating Work

- Establish an Earned Income Tax Credit ("EITC") — March 2016
  - Establish an EITC that, like the federal EITC, targets families with children, headed by working age persons, to stimulate employment among low-wage workers, reduce informal economy activities, bring families into the tax system and offset sales tax regressivity
    - Cost after full implementation will be ~$150 million per year
    - Former Commonwealth EITC program (2006-2014) did not differentiate among claimants by filing status, presence of dependents or age of the tax filers

- Reform Nutritional Assistance Program ("NAP") Benefits — March 2016
  - Request US Department of Agriculture ("USDA") to extend gross income exception for the receipt of NAP benefits from 12 to 18 months to allow more time for employees to experience salary and benefits increases that outweigh loss of NAP benefits
  - Modify NAP income thresholds for the Commonwealth so that program participants experience a more gradual and income-targeted reduction in NAP benefits when entering the workforce to eliminate the current cliff effect on benefit reduction

Economic Growth and Structural Reform

Economic Growth and Structural Measures	Target Date

1.1 Stimulate Employment and Labor Force Participation (cont.)

- Public Housing and Section 8 — June 2016
  - Apply to US Department of Housing and Urban Development ("HUD")'s "Moving to Work" program to receive waivers of rules that govern public housing and federal Section 8 voucher program
    - Program's goal is to give incentives to families with children, where the head of household is working, seeking work, or is preparing for work to obtain employment, becomes economically self-sufficient and increase housing choices for low income families
      - After receiving waiver, local Housing Department to develop rent structures that allow residents to increase their earnings through work without penalty
  - Apply to HUD's "Jobs Plus Pilot Program" — October 2015
    - Program incentivizes employment through income-disregards for working families, and provides a set of services designed to support work including employer linkages, job placement and counseling, educational advancement, and financial counseling

- Integrate Childcare Services
  - Integrate Family Department's child care and Head Start programs with the Puerto Rico Department of Education's Pre-K program in local public schools in order to reduce transportation costs for working families with multiple children and provide such families with full day childcare options — July 2016
    - Cost of program under evaluation

Minimum Wage

- To promote the hiring of young workers, request Congress to grant a 10-year waiver from future minimum wage increases for workers aged 25 and younger. This increase to the minimum wage would apply to any individual worker after 2 years — November 2015

- Grant the petition by the Commonwealth to exempt Puerto Rico from the US Department of Labor proposal to increase the salary level for required exemption under the Fair Labor Standards Act ("FLSA") referred to as "EAP" or "white collar" exception, which would increase the salary threshold for exempt employees that are full time salaried employees to $50,440 annually — January 2016

Economic Growth and Structural Reform

Economic Growth and Structural Measures	Target Date
1.2 Diversify Fuel Base and Stabilize Energy Rates	

Lack of fuel diversification, mismanagement and lack of energy policy continuity have resulted in **high energy costs**, **eroding the Commonwealth's competitiveness** and increasing the cost of doing business

▪ Complete restructuring of Puerto Rico Electric Power Authority's ("PREPA") capital structure and operations to produce cash flow relief during next five years to invest in necessary infrastructure and stabilize rates ❖ On September 1, 2015, PREPA announced that it had reached an agreement in principle with the Ad Hoc Group of PREPA bondholders – comprised of traditional municipal bond investors and hedge funds that hold approximately 35% of PREPA's outstanding bonds – regarding the economic terms of a restructuring of a significant portion of PREPA's bond debt. PREPA's agreement with the Ad Hoc Group marks PREPA's first agreement with a significant financial stakeholder regarding the substantive terms of its financial transformation. PREPA will continue negotiating with its financial guaranty bond insurers and revolving fuel line lenders, with the goal of reaching an agreement on a consensual recovery plan among all of its major financial stakeholders	To be determined
▪ Issue request for proposal ("RFP") to third-party investors to upgrade existing generation capacity and build new, more efficient generation plants, allowing PREPA to transition into a transmission and distribution company	2016 (1)
▪ Depoliticize PREPA by attracting professional external management and directors	2016 (1)
▪ PREPA to invest more than $2 billion over the next five years to upgrade vital generation, transmission and distribution infrastructure	2015-2020

(1) Contingent on timing of PREPA's restructuring.

Economic Growth and Structural Reform

Economic Growth and Structural Measures	Target Date

1.3 Implement Pro-Growth Corporate Tax Regime

The Commonwealth's current corporate tax regime is too complex, distorts economic choices and produces horizontal inequities. Puerto Rico must **institute a pro-growth tax regime** applicable to all companies doing business on the island that **lowers nominal tax rates and eliminates loopholes and unnecessary complexity**

- Enact legislation to amend Puerto Rico's Internal Revenue Code to implement flatter, lower-rate corporate tax regime for both new and existing companies — March 2016
  - Reduce nominal corporate tax rates
  - Eliminate inefficient corporate deductions and tax credits; eliminate or reduce alternative minimum tax
    - Simplified corporate tax regime would reduce unnecessary compliance burdens on entrepreneurs
- Enact legislation, after dialogue with existing multinationals, to retain and attract foreign direct investment — March 2016
  - Legislation would amend Act 154-2011 to extend the 4% excise tax for an additional 5-year period to stabilize the General Fund's revenue base(1)
  - With respect to foreign multinationals, legislation would also amend Act 73-2008 and be applicable to new companies coming to Puerto Rico, existing companies wishing to convert to new tax regime and all firms after the expiration of their current tax grants
  - New regime would seek to substitute Act 154-2011 excise tax and its revenues without increasing overall tax liability to existing companies, including foreign companies that currently do not credit the excise tax against federal income

(1) For Act 154 extension 5-year revenue projections, please refer to measure 2.2 of the Fiscal Stability section.

Economic Growth and Structural Reform

Economic Growth and Structural Measures	Target Date
1.3 Implement Pro-Growth Corporate Tax Regime (cont.)	
▪ Request Congress to provide Puerto Rico with tax treatment that encourages US investment on the island, such as:	November 2015
- Section 933A: Amend US Internal Revenue Code to add new Section 933A to permit US-owned businesses in Puerto Rico to elect to be treated as US domestic corporations	
- Economic Activity Tax Credit: Enact an economic activity tax credit for US investment in Puerto Rico designed as a targeted, cost-efficient version of former Section 936 of the US Internal Revenue Code	
- Base Erosion: In the event the US moves towards a territorial taxation system, exempt Puerto Rico from base erosion and/or minimum tax measures	

Economic Growth and Structural Reform

Economic Growth and Structural Measures | **Target Date**

1.4 Reduce Costs and Improve Ease of Doing Business

Puerto Rico has been losing competitiveness as measured by global reports produced by the World Economic Forum and the World Bank. To jumpstart its economy, **Puerto Rico must be equipped with a business-friendly environment that is conducive to sustained economic growth**

- Centralize and streamline permitting process
  - Submit legislation to: — January 2016
    - Centralize all permit application processes in the Office of Management of Permits ("OGPe"), providing a single access point and electronic permit interface for all agencies and municipalities
    - Where a federal environmental review procedure is required, integrate concurrent local agency review and make the federal record of decision ("ROD") binding on local agency ruling to lower costs and avoid inconsistent administrative rulings
    - Provide for a 7-day agency response period for "Categorical Exclusions" (e.g. minor lot designation variations for low impact environmental construction works); applications deem granted if agency has not ruled on permit during said period
    - Require municipalities to adopt simplified uniform general permitting regulation~~s~~ ("*Reglamento Conjunto*")
  - Issue Executive Order to expedite planning, permitting and environmental review procedure for high-priority projects, including high-impact infrastructure projects outlined in the FEGP — November 2015
  - Consolidate Environmental Quality Board, Solid Waste Authority and Natural and Environmental Resources Department in order to simplify and streamline the environmental review process — April 2016
  - Adopt a joint general construction permit and expedited application procedure for "low impact" construction projects — April 2016

Economic Growth and Structural Reform

Economic Growth and Structural Measures	Target Date
1.4 Reduce Costs and Improve Ease of Doing Business (cont.)	
▪ Modernize property registry	November 2015
- Pass House Bill No. 2479 to implement 100% digital, electronic and paperless property registry platform	
❖ Platform expected to be effective upon legislative approval	
▪ Reduce transportation costs	
- Ask Congress to repeal Jones Act's application to the Commonwealth in order to reduce maritime transport costs to the island	October 2015
• Request temporary administrative waiver from US Government in energy related transports	November 2015
- Review current ground transportation regulatory framework	

Economic Growth and Structural Reform

Economic Growth and Structural Measures | **Target Date**

1.5 Invest in Strategic Infrastructure

The Commonwealth's infrastructure assets (ports, roads, bridges) are in need of substantial capital investments due to limited financial resources and historically insufficient maintenance. In order to grow the economy, the Commonwealth must **increase spending on capital expenditures** to strengthen its infrastructure system and allow it to continue to serve as a pillar of economic growth. **Given the tight fiscal situation, the Commonwealth should leverage P3s to help achieve its capital expenditure goals**

- Central government to use cash from operations to invest approximately \$3.3 billion(1) during the five-year growth and adjustment period to improve infrastructure, boost aggregate demand and implement structural and fiscal measures — 2015-2020 (annual targets)
  - Government to begin budgeting for capital expenditures as part of General Fund budget
  - Capital expenditures ("capex") program designed to leverage federal matching funds, prioritize projects with economic impact and provide adequate maintenance to public infrastructure, including buildings, roads and bridges
    - Total investment including federal matching funds, amount to ~\$7.7 billion
- In addition to directly funding its capital improvement program, the Commonwealth will seek to leverage P3s to build, maintain and operate new and legacy infrastructure, including electricity generation plants and transportation assets — 2015-2020 (annual targets)
- Strategic infrastructure projects (financed by government, federal and/or private funds) include: — 2015-2020 (annual targets)
  - Roads: Extension of Northwest Highway Corridor, PR-10
  - Airports and Ports: Upgrade Piers 1 and 4, Terminal, Roadway and Taxiways in Aguadilla Airport, Port of the Americas, Dry Dock, Army Terminal, Maintenance Dredging in San Juan Bay
  - Health: Science District (including cost to complete Comprehensive Cancer Center)
  - Strategic: Roosevelt Roads; investments in other strategic sectors (e.g. aerospace)
  - Other: Flood control projects, necessary rehabilitation and maintenance of roads and other public assets

(1) FEGP projections contemplate this investment in maintenance and strategic capex.

Economic Growth and Structural Reform

Economic Growth and Structural Measures	Target Date

1.5 Invest in Strategic Infrastructure (cont.)

- Independent public enterprises, such as PREPA and PRASA, will separately undertake significant capex programs — 2015-2020 (annual targets)
  - PREPA plans to invest more than $2 billion over the next five years to upgrade vital generation, transmission and distribution infrastructure, including the Aguirre Offshore Gas Port ("AOGP")
    - PREPA restructuring process expected to release sufficient resources to undertake capex program
    - PREPA submitted a loan application to the US Department of Energy ("DOE") 1703 Program to finance a portion of AOGP
  - PRASA also contemplates financing approximately $1.4 billion in capex during the same period for water/waste water infrastructure renewal and replacement, water loss control and technology, among others
- Leverage federal resources through the Build America Transportation Investment Center on transportation related infrastructure projects and P3 proposals

Fiscal Stability – Revenue Enhancing Measures

"Given looming revenue and spending pressures, eliminating the fiscal deficit will take substantial measures. Reforms should aim more at broadening tax bases than raising rates, and at targeted expenditure reduction rather than across-the-board cuts. But even a major fiscal effort leaves large residual financing gaps that will need to be bridged with debt relief." –the Krueger Report p.19

Revenue Enhancing Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

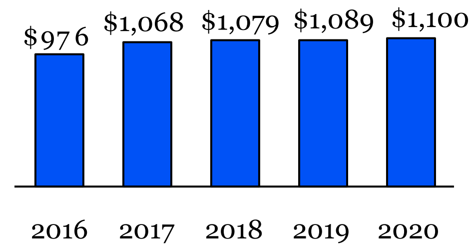
2.1 Complete Transition to VAT

In order to decrease tax evasion and increase the revenue capture rate, the Commonwealth must place greater reliance in consumption taxes and move towards VAT. **On May 29, 2015, the Government enacted Act 72-2015, which increases the SUT rate from 7.0% to 11.5%, expands the tax base by taxing certain business to business ("B2B") services and provides for a VAT** to substitute the Central Government's portion of the SUT

Increase SUT Rate

- Starting July 2015, transactions that were subject to the 7% SUT are now subject to an 11.5% SUT, with the entire 4.5% increase going to the Central Government[1]

Completed



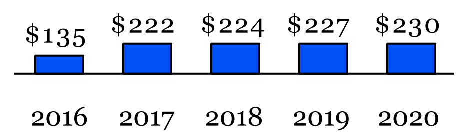
Taxing B2B Services and Transitioning to VAT System (Incremental to SUT Rate)[1]

- Starting October 2015, B2B transactions that are currently taxable will be subject to an 11.5% SUT; B2B transactions and professional services that were previously exempt from the SUT will be subject to a 4% SUT

October 2015

- Starting April 2016, all transactions subject to the SUT will be subject to a new VAT of 10.5% plus a 1% municipal SUT

April 2016



(1) Numbers shown are the estimated benefit to the General Fund.

Fiscal Stability – Revenue Enhancing Measures

Revenue Enhancing Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

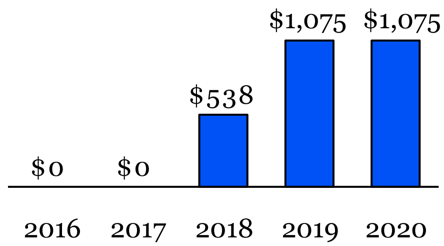
2.2 Stabilize Corporate Tax Revenue Base

The Commonwealth is currently highly dependent on Act 154-2011 excise tax receipts (approximately 20% of general fund revenues). The 4% excise tax is due to be replaced by a "Modified Source Income Rule" tax in December 2017 (FY 2018) and an extension of the 4% tax rate is necessary to ensure revenue certainty during fiscal and economic adjustment period

- Extend Act 154-2011 4% excise tax for an additional 5-year period as existing multinationals transition to a new corporate tax regime

  March 2016

- Amend, after consultation with existing multinationals, the Internal Revenue Code and Act 73-2008, to establish a new corporate tax regime that substitutes the Act 154-2011 excise tax and its revenues without increasing overall tax liability to existing companies



Note: Incremental impact vs. Krueger Report's "Loss of Act 154" downside risk as modified by Adjusted Estimates

Fiscal Stability – Revenue Enhancing Measures

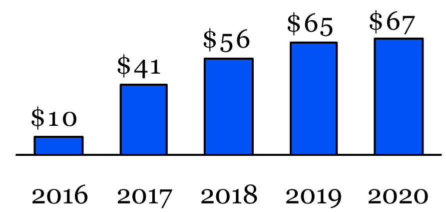
Revenue Enhancing Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

2.3 Improve Tax Administration and Enforcement

The Commonwealth lacks a robust, modern and effective tax administration, resulting in significant tax evasion and high taxpayer compliance and administrative costs

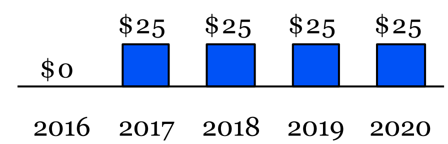
- Leverage technology and training in order to increase capture rates and improve tax administration and enforcement, including:
  - Improve Integrated Merchant Portal System (“PICO”)
  - Implement Automated System for Customs Data (“ASYCUDA”)
  - Expand alternative delivery and payment channels’ capabilities
  - Transform Collection Centers into Integrated Service Centers
  - Joint-ventures with Municipalities for SUT oversight
  - Implement performance management, develop work plans and create Professional Development Institute

2016-2020 (annual targets)



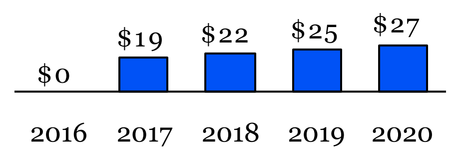
- Restrict use of tax amnesties and closing agreements to increase revenue certainty and reduce tax evasion

June 2016



- Tackle widespread use of illegal video lottery machines that erode Puerto Rico’s tax base by implementing and enforcing tax on, and regulating, video lottery games(1)

March 2016



Note: All impact estimates are net of investments.
(1) Net of transfers as required by law.

Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

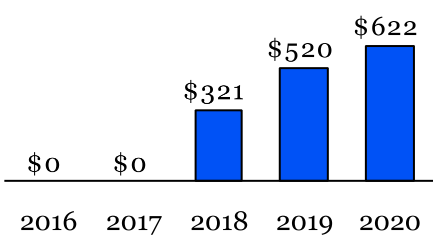
2.4 Reduce Operating Costs

Despite significant efforts to **reduce central government expenses** through headcount attrition, freezing formula-based appropriations, service costs and collective bargaining agreements, among other measures, the Commonwealth's upcoming fiscal challenges, including unfunded retirement systems and increasing health care costs, **will require further expense cuts in governmental subsidies, a gradual reduction in payroll expenses and the implementation of additional operational efficiencies**

Act 66

- Extend until FY 2021 Act 66-2014's freeze of new hires, formula-based appropriations, service costs, increase in salaries and collective bargaining agreements(1)

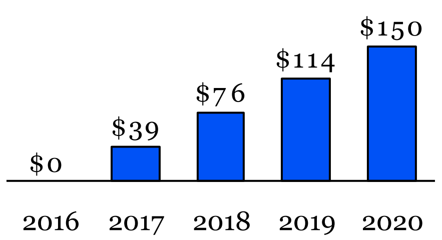
Target Date: December 2015



Human Resources

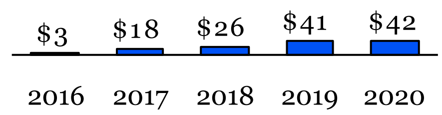
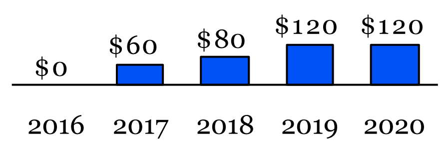
- Reduce payroll costs by implementing a 2% annual attrition target(1)(2)
  - To achieve attrition target, the Office of Management and Budget ("OMB") may offer early retirement window to selected public sector employees
  - Commonwealth may use a portion of the proceeds of P3 initiatives to incentivize voluntary retirement

Target Date: 2016-2020 (annual targets)



(1) Impact does not include the negative effect on Additional Uniform Contribution to the public pension systems.
(2) Totals excludes Puerto Rico Department of Education ("PRDE"). Attrition target with respect to PRDE is included in Section 2.6 hereto.

Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)
2.4 Reduce Operating Costs (cont.)		
▪ Align public sector vacation and sick leave benefits for new hires with the highest benefits for the private sector	November 2015	Estimated impact to be determined
▪ Implement new government-wide employee classification program to improve mobility, better allocation of human resources and uniform salaries for the same positions across all government so as to continue benefiting from headcount attrition	June 2016	Estimated impact to be determined
<u>Operational Efficiencies</u>		
▪ Adopt and complete implementation of both: (i) Government reorganization and Efficiency Plan[(1)], as developed by the OMB and the Department of State, so as to consolidate local government offices, increase use of technology and shared services, and (ii) redesign of governmental structures proposed by OMB and UPR	2016-2020 (annual targets)	
<u>Procurement</u>		
▪ Achieve ~4% economies of scale and efficiencies by establishing a modern, centralized procurement system in the Puerto Rico General Services Administration ("GSA") for all purchases greater than $25,000 (currently $195,000) ▪ Federal legislation granting the Commonwealth and its agencies access to the GSA Cooperative Purchasing program and all federal supply schedules	June 2016	

(1) Executive Order OE-2015-23.

Fiscal Stability – Expense Reduction Measures

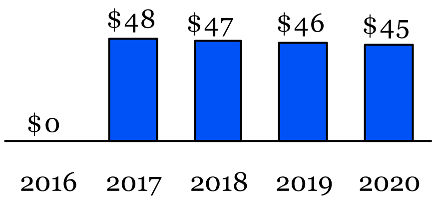
Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

2.4 Reduce Operating Costs (cont.)

Teacher's Retirement System

June 2016

- Supreme Court opinion ruled that certain sections of Act 160 can only be applied prospectively to newly hired teachers. Further changes to the TRS are required to ensure the payment of benefits for years to come. Accordingly, TRS is working closely with actuaries towards a reformed proposal that ensures payment of benefits to existing retirees while passing constitutional scrutiny and that considers increases to employee contributions and/or modifications to special law benefits



Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

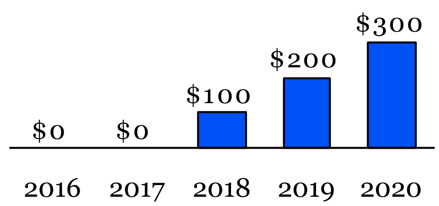
2.5 Cut Government Subsidies

The central government's precarious fiscal situation is exacerbated by the **sizable appropriations to independent government entities including municipalities and UPR.** For FY 2015, the government allocated almost 18% of its General Funds in appropriations to independent entities while significantly reducing the budget for the central government

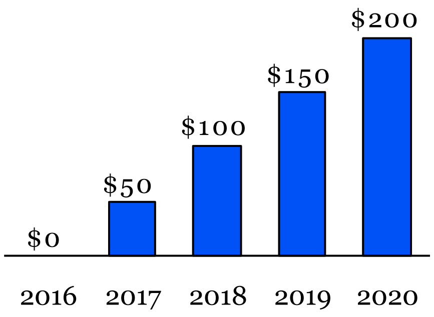
Municipalities

- Enact legislation to, beginning FY 2018, gradually adjust subsidies provided to municipalities by the central government, while empowering municipalities with the proper legal, administrative and operational tools for them to offset such decrease
  - Municipalities may present revenue generation and expense reduction initiatives, that may include changes to municipal license fees, modernization of property tax regime and municipal consolidations, among others
  - Central government to commission a study to provide analysis of, and recommendations with respect to, the relevant alternatives

March 2016



Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)
2.5 Cut Government Subsidies (cont.)		
<u>University of Puerto Rico</u>		
▪ The UPR shall develop, in consultation with GDB as fiscal agent, a plan to ensure the continuous delivery of a world-class education in the context of its institutional autonomy, the fiscal environment of the Commonwealth and its historical role as a promoter of the island's economic development	January 2016	
❖ The UPR has alternatives to operate in a more cost-effective manner, without impacting low-income students, such as means-testing tuition, operational efficiencies, employment attrition and maximizing federal funding		
▪ Enact legislation to gradually adjust revenue base underlying general fund formula-based appropriations to the UPR in order to exclude debt service and pension costs	June 2016	
❖ For FY 2016, the Commonwealth budget provides an $834 million subsidy to the UPR (in addition to ~$62 million from casino slot revenues plus $35 million in other direct appropriations), which constitutes over two thirds of the UPR's total budget		
❖ Effect of adjustment on UPR's formula is additive to the effect of the proposed extension of Act 66-2014, which freezes the formula-based appropriation to the UPR		
▪ Pass legislation to redirect to Health Insurance Administration ("ASES") the casino slot revenues currently assigned to the UPR in order to fund current Commonwealth health care coverage to medical poor beneficiaries who do not qualify for Medicaid[1]	June 2016	

(1) Casino slot machine revenue has been declining over the last years.

Fiscal Stability – Expense Reduction Measures

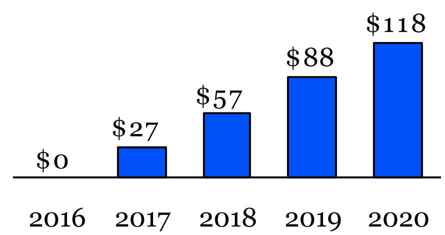
Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

2.6 Right-Size Department of Education

Since 1980, **enrollment at public schools has declined 41% and, due to demographic trends, it is expected to fall an additional 25% (~317,000 students) by 2020.** This decline has led to a reduction in school utilization and a decrease in the **student to teacher ratio to 12:1 (US average is 16:1).** The Puerto Rico Department of Education has made significant progress during the last two years by **consolidating 135 schools** and reducing the number of temporary teachers by more than **1,000**

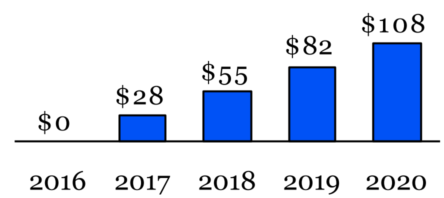
- Consolidate public schools based on specific parameters such as enrollment, school utilization and distance to adjust PRDE's facilities to current demographic trends and improve student-to-teacher ratio for both underutilized and overcrowded schools
  - The PRDE has made significant progress over the last two years in adjusting its human capital and physical infrastructure to its fiscal and demographic reality. As it continues to right-size its resources, the PRDE will ultimately position itself to deliver high quality education with well compensated teachers

2017-2020 (annual targets)



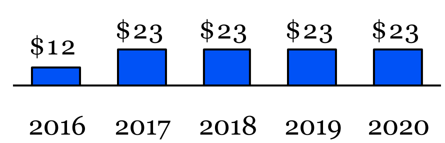
- Reduce PRDE's payroll through 2% attrition[(1)]

2017-2020 (annual targets)



- Complete remaining phases of PRDE's ongoing restructuring plan, which requires overhauling the PRDE's management and operations and reducing expenditures on select private services

2016-2020 (annual targets)



- Consider selected asset sales, including the Commonwealth's real estate asset portfolio, to finance retirement windows for teachers and/or capitalize severely underfunded Teachers Retirement System

2016-2020

Estimated impact should be determined by March 2016

(1) Attrition calculated net of impact attrition measure in Section 2.4 hereto; impact does not include the negative effect of Additional Uniform Contribution to Teachers Retirement System.

Fiscal Stability – Expense Reduction Measures

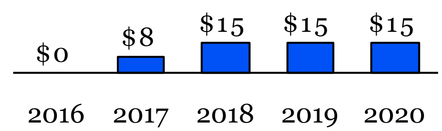
Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)

2.7 Control Health Care Costs

The Commonwealth's public health care plan covers approximately 1.6 million beneficiaries (all but 180,000 of which are not covered by Medicaid) and is financed by a combination of federal and local funds.(1) Puerto Rico ranks #14 nationally in terms of total Medicaid enrollment and #1 as a percentage of population enrolled (48%). While the Commonwealth **is subject to a federal spending cap that limits federal dollars for Medicaid to approximately $260 million (excluding $150 million for the Children's Health Insurance Program "CHIP"), there is no cap for US states. Puerto Rico also faces a "health care cliff," currently estimated to grow to $1.7 billion dollars by 2020, upon the exhaustion of Affordable Care Act funding in FY 2018**

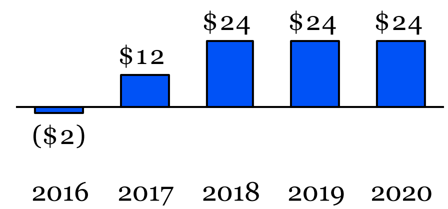
- Implement "STAR"-like(3) rating system and establish a provider payment scale based on performance

October 2015



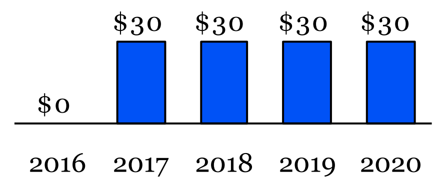
- Implement functional P3s at state hospitals (billings, admissions, maintenance and food services among other support services), to bring best in class practices, centralize functions and streamline processes (e.g. surgery cancellations; efficient emergency room management)(4)

July 2016



- Standardize health protocols and establish uniform fee schedules
  - Create uniform guide for medical procedures and corresponding medical service fee schedule

July 2016



(1) Federal funds would include funds from Medicaid, CHIP and Medicare Advantage programs.
(2) Coverage will be suspended to those who do not pay the premium; impact is net of incremental operation costs.
(3) Centers for Medicare and Medicaid Services ("CMS") Five Star Quality Rating System.
(4) Estimates are based on current P3 billing experience at University District Hospital ("UDH"). Estimates are net of incremental operating costs.

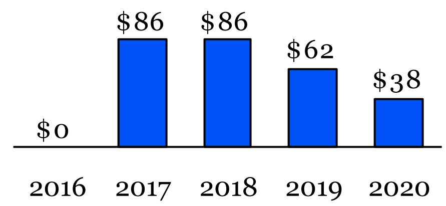
Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures | **Target Date** | **Estimated Incremental Impact FYs** ($ millions)

2.7 Control Health Care Costs (cont.)

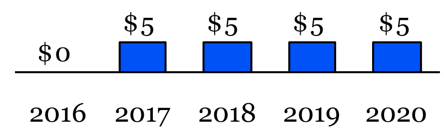
- Amend Act 72-1993 to ensure transfer of municipal contributions to ASES (preventing withholding contributions), along with their corresponding federal match[(1)], and clarify FY 2005 as the base year to calculate municipal contributions

February 2016



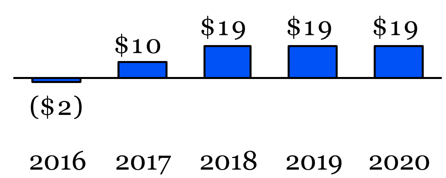
- Rationalize number of federally qualified health care centers receiving grants under Section 330 of the Federal Pubic Health Service Act that are located near existing hospitals or clinics

July 2016



- Create the Puerto Rico Medical Center Campus organized around specialty institutions by integrating all government hospitals into a single organization[(2)]
  - Phase 1 contemplates merging Administration of Medical Services of Puerto Rico (“ASEM”), the University Hospital and University Pediatric Hospital (“HOPU”)
  - Phase 2 would merge the Industrial Hospital (“Hospital Industrial”) currently run by the State Insurance Fund, along with other government run hospitals

December 2016



(1) Federal matching decreases as ACA funds deplete over time.
(2) Savings are obtained by economies of scale in purchasing, maintenance and other central support functions. Saving are estimated at 5% of each hospital’s budget.

Working Group for the Fiscal and Economic Recovery of Puerto Rico

Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures	Target Date	Estimated Incremental Impact FYs ($ millions)
2.7 Control Health Care Costs (cont.)		
▪ Obtain equitable Medicare and Medicaid treatment and funding from US Government	December 2017	Financial impact subject to timing and nature of federal policy

Medicaid

- Remove statutory limits on Medicaid funding, including not setting the Federal Medical Assistance Percentage ("FMAP") at a fixed percentage
  - Puerto Rico's Medicaid funding level is capped at approximately $260 million and its FMAP rate set at 50%, which per Puerto Rico's income levels should be 83%

Medicare

- Reimburse Puerto Rico hospitals who admit patients under the Inpatient Prospective Payment System ("IPPS") at the same rate as mainland hospitals
- Make Puerto Rico hospitals eligible for bonus payments under Medicare
- Automatically enroll in Medicare Part B individuals enrolled in Medicare Part A
- Provide Puerto Rico doctors fair treatment under the Practice Expense Geographic Practice Cost Index ("GPCI") payment formula
- Ensure adequate per member per month ("PMPM") payments to Medicare Advantage plans in Puerto Rico
- Allow adequate utilization of Enhanced Allotment Program ("EAP") prescription drug funding

Medicaid and Medicare

- Extend to Puerto Rico Medicaid and Medicare disproportionate share hospital ("DSH") program allotments

Fiscal Stability – Expense Reduction Measures

Expense Reduction Measures	Target Date
2.8 Leverage P3s to Deliver Quality and Cost-Efficient Services	

The need for **proper infrastructure construction and maintenance, necessary for economic growth, can be met by leveraging public private partnerships**. Recent positive experience with the LMM Airport and PR-22 Highway demonstrate that P3s are a viable model and an effective tool to rehabilitate and develop necessary infrastructure, reduce operational costs and improve governmental services for the Commonwealth

Measure	Target Date
▪ Concession remaining toll roads, including PR-20, PR-52 and PR-66 in consultation with US Department of Transportation - Improve, intra-Island connectivity, road and bridge quality, and travel safety. Continuous investment in and maintenance of the roads would be mandatory as set forth in a Concession Agreement - Concessions would help transform HTA into a contract administrator and limit its construction role	(estimated impact subject to terms of concession)
▪ Merge Public Building Authority and Office for the Improvements of Public Schools ("OMEP") - Transform PBA into a more efficient and effective public corporation; consider transferring the construction function to ("PRIFA") to avoid duplication of functions	(estimated impact subject to terms of concession)
▪ P3 maritime transport and bus system operations - Maritime: 5-year minimum concession agreement for the operation and maintenance of the public maritime transportation services - AMA: currently evaluating possible transfer of operations to municipalities and potential P3 transactions	(estimated impact subject to terms of concession)
▪ Evaluate potential concessions for ports and airport operations or facilities, and work with the Federal Aviation Administration ("FAA") to consolidate underutilized or geographically unnecessary airports	(estimated impact subject to terms of concession)
▪ Identify and pursue additional P3 opportunities	

Institutional Reform and Transparency

"The legacy of budgetary laxity, non-transparency, and unreliable/dated statistics must be overcome if the reform program is to work and command credibility. The priorities include a rolling 5-year budgetary plan approved by the legislature, legislative rules to limit changes to the plan, an independent fiscal oversight board to advise on the budget and control its implementation, and strengthening the quality and timeliness of economic data." –The Krueger Report p.22

Institutional Reform and Transparency Measures	Target Date

3.1 Install New Accounting and Financial Systems

The central government's financial and payroll systems are obsolete and can not communicate with the systems of principal agencies, such as the PRDE and the Health Department. Lack of integration of agencies under the same platform hinders the ability to timely monitor expenses, complete annual audits and publish accounting financial statements

- Implement new financial/accounting and payroll system that unifies the patchwork of governmental platforms, which affect the government's ability to properly monitor its fiscal situation and result in material delays in the preparation of financial information — July 2017
  - Contract system provider (implementation schedule is expected to be approximately 18 to 24 months) — November 2015
  - Requires an approximate investment of at least $25 million to $40 million

3.2 Establish Centralized Single Treasury Function

The Commonwealth currently has a **highly fragmented treasury system** that places **weak emphasis on ensuring fiscal and financial controls** and provides little visibility of the Government's consolidated financial position. The centralization of treasury functions in the central government can provide significant communication, visibility and efficiency benefits

- Establish by legislation centralized single treasury functions across Commonwealth agencies and dependent public corporations to enhance visibility, reduce financing costs and improve cash flow — June 2016
  - Identify agencies and component units that would be part of the centralized structure — January 2016
  - Build the necessary infrastructure for the monitoring and projection of cash flows — June 2016
  - Enact legislation to create centralized treasury with provisions that would allow for enforcement — June 2016

Institutional Reform and Transparency

Institutional Reform and Transparency Measures	Target Date

3.3 Improve Fiscal and Economic Decision-Making

Investors, bondholders, policymakers, and academics have repeatedly pointed to the need of equipping the Commonwealth with more **transparent, reliable and timely macroeconomic data** that complies with global standards. A methodological modernization of the Commonwealth's national accounts is long overdue, along with a **centralized and well-structured approach towards financial and economic development decisions**

- Adopt the Institute of Statistics and the Planning Board 5-year plan to strengthen the economic statistical system and analysis by modernizing national accounts with an estimated investment of $3 million per year — 2015-2020 (annual targets)
  - Reorganize and expand Puerto Rico's current 5 national accounts into 7 accounts (Net Income and Gross Product, Personal Income and Outlays, Government Receipts and Expenditures, Foreign Transactions-Current, Foreign Transactions-Capital, Gross Savings and Investment and Private Sector Income)
  - Present the national accounting statistics in accordance with the 2008 United Nations standards
  - Develop a new forecasting model for Puerto Rico's national accounts
  - Publish official full-set of quarterly national accounting statistics that is consistent with annual estimates
  - Request technical assistance from the US Bureau of Labor Statistics and the US Bureau of Economic Analysis
- Consolidate the functions of the Treasury Department, OMB and the GDB's non-core banking operations into new Finance and Public Credit Department to better manage and coordinate fiscal and financial policy — June 2017
  - Existing fiscal and financial policy is heavily fragmented; international best practices typically consolidate revenue, budget and financial functions to obtain a government-wide visibility and improve execution
- Reorganize the Department of Economic Development and Commerce to better deploy economic promotion resources and shared corporate services
  - Complete DDEC organizational diagnostic with respect to corporate governance, organizational structure, decision-making processes and return on investment philosophy — February 2016
  - Submit and pass legislation to implement new DDEC organizational structure and business plan — January 2017

Institutional Reform and Transparency

Institutional Reform and Transparency Measures	Target Date

3.3 Improve Fiscal and Economic Decision-Making (cont.)

- Merge strategic public corporations into a real estate development agency that supplements the Department of Economic Development to improve economic and business planning — September 2016
  - Centralized entity will serve as a project management coordinator while leveraging resources from current entities and minimizing operational costs via shared services
  - Request to the US Census Bureau that Puerto Rico be included in the Census of Governments and that the National Agricultural Statistical Service provide technical assistance developing agricultural surveys

3.4 Implement New Budgetary Rules

Given that the Commonwealth has suffered from chronic **budget deficits** and has repeatedly failed to meet budgetary estimates, it should institute new budgetary rules and practices to impose budgetary discipline and help achieve FEGP targets

- Refer to Summary of Fiscal Responsibility and Economic Revitalization Act of the FEGP

3.5 Institute Control Board for Policy Continuity and Compliance

An independent **fiscal control board, comprised by experienced individuals** from inside and outside the Commonwealth, **shall oversee the implementation of the 5-year FEGP** with the powers necessary to ensure compliance

- Refer to Summary of Fiscal Responsibility and Economic Revitalization Act of the FEGP

Requests to the US Government

Federal action is necessary to place Puerto Rico on a sustainable path

Type	Request	Needed for Measure
Long-Term Sustainability	▪ Access to a legal framework to restructure the Commonwealth's liabilities in an orderly process	Financing Gaps
	▪ Equitable Medicare and Medicaid treatment and funding Medicaid - Remove statutory limits on Medicaid funding, including not setting the Federal Medical Assistance Percentage ("FMAP") at a fixed percentage ❖ Medicaid funding level is capped at ~$260 million and the FMAP rate set at 50%, which equals an effective rate of 15% to 20%, whereas according to Puerto Rico's income levels should be 83% Medicare - Reimburse Puerto Rico hospitals who admit patients under the Inpatient Prospective Payment System ("IPPS") at the same rate as mainland hospitals - Make Puerto Rico hospitals eligible for bonus payments under Medicare - Automatically enroll in Medicare Part B individuals enrolled in Medicare Part A - Provide Puerto Rico doctors fair treatment under the Practice Expense Geographic Practice Cost Index ("GPCI") payment formula - Ensure adequate PMPM payments to Medicare Advantage plans in Puerto Rico - Allow adequate utilization of Enhanced Allotment Program ("EAP") prescription drug funding Medicaid and Medicare - Extend Medicaid and Medicare disproportionate share hospital ("DSH") program payments	2.7 Control Health Care Costs
	▪ Maintain Act 154-2011 excise tax creditability for the duration of the FEGP period	2.2 Stabilize Corporate Tax Revenue Base
	▪ Exemption from Jones Act application to reduce transportation costs and increase competitiveness	1.4 Reduce Costs and Improve Ease of Doing Business

Working Group for the Fiscal and Economic Recovery of Puerto Rico

Requests to the US Government (cont.)

Federal action is necessary to place Puerto Rico on a sustainable path

Type	Request	Needed for Measure
Long-Term Growth	▪ Provide Puerto Rico with a tax treatment that encourages US investment on the island, such as: - Section 933A: Amend US Internal Revenue Code to add new Section 933A to permit US-owned business in Puerto Rico to elect to be treated as US domestic corporations - Economic Activity Tax Credit: Enact an economic activity tax credit for US investment in Puerto Rico designed as a targeted, cost-efficient version of former Section 936 of the US Internal Revenue Code - Base Erosion: In the event the US moves towards a territorial taxation system, exempt Puerto Rico from base erosion and/or minimum tax measures	1.3 Implement Pro-Growth Corporate Tax Regime
	▪ Flexibility on minimum wage with respect to young workers ▪ "White collar" exemption under Fair Labor Standards Act ("FLSA") ▪ Pro employment requests with respect to NAP and public housing programs	1.1 Stimulate Employment and Labor Force Participation
Near-Term Impact Measures	▪ FAA approval for any airport consolidations ▪ Executive approval or Congressional authorization to sell accumulated Federal Highway toll credits	2.8 Leverage P3s to Deliver Quality and Cost-efficient Services
	▪ Technical assistance from the Census Bureau and National Agricultural Statistical Service	3.3 Improve Fiscal and Economic Decision-Making
	▪ DOE financing for Aguirre Offshore Gas Port. Finalize remaining AOGP federal permits ▪ Technical Assistance from the Build America Transportation Investment Center on transportation related infrastructure projects and P3 proposals	1.5 Invest in Strategic Infrastructure
	▪ Federal legislation granting the Commonwealth and its agencies access to the GSA Cooperative Purchasing program and all federal supply schedules	2.4 Reduce Operating Costs

Summary of Measures – Revenue

A summary of the annual impact of the various revenue measures as determined by the Working Group is presented below

$ millions	2016P	2017P	2018P	2019P	2020P	Total
Revenue Measures						
2.1 Complete Transition from Original SUT to Increased SUT/VAT	**$1,111**	**$1,290**	**$1,303**	**$1,316**	**$1,330**	**$6,350**
2.2 Stabilize Corporate Tax Revenue Base	**–**	**–**	**538**	**1,075**	**1,075**	**2,688**
2.3 Improve Tax Administration & Enforcement						
Leverage Tech and Training to Increase Capture Rates and Improve Tax Admin	10	41	56	65	67	239
Restrict Use of Tax Amnesties and Closings	–	25	25	25	25	100
Video Lottery	–	19	22	25	27	93
Improve Tax Administration & Enforcement	**10**	**85**	**103**	**115**	**119**	**432**
Total Revenue Measures	**$1,121**	**$1,375**	**$1,943**	**$2,506**	**$2,524**	**$9,469**
Memo: Total Revenue Measures ex. Increased SUT/VAT Already Enacted	*$10*	*$85*	*$640*	*$1,190*	*$1,194*	*$3,119*

Summary of Measures – Expense

A summary of the annual impact of the various expense measures as determined by the Working Group is presented below

$ millions	2016P	2017P	2018P	2019P	2020P	Total
Expense Measures						
2.4 Reduce Operating Costs						
Extend Law 66	–	–	$321	$520	$622	$1,463
Employee Attrition	-	39	76	114	150	378
Reclasification of Positions	-	-	-	-	-	-
Reduction in Licenses	-	-	-	-	-	-
Operational Efficiencies	3	18	26	41	42	130
Centralized Procurement	-	60	80	120	120	380
Retirement Plans	-	48	47	46	45	186
Reduce Operating Costs	**3**	**165**	**550**	**840**	**979**	**2,537**
2.5 Cut Governmental Subsidies						
Municipalities	-	-	100	200	300	600
UPR	-	50	100	150	200	500
Cut Governmental Subsidies	**-**	**50**	**200**	**350**	**500**	**1,100**
2.6 Right-Size Department of Education						
Consolidate Schools	-	27	57	88	118	290
Reduce Department's Payroll through Attrition	-	28	55	82	108	272
Complete Remaining Phases of PRDE Restructuring Plan	12	23	23	23	23	104
Right-Size Department of Education	**12**	**78**	**135**	**193**	**249**	**666**
2.7 Control Health Care Costs						
Implement STAR Ratings System and Scale Payments	-	8	15	15	15	53
Implement Functional P3s at State Hospitals	(2)	12	24	24	24	82
Standardize Health Protocols and Impose Uniform Fee Schedules	-	30	30	30	30	120
Restore Municipal Contributions and Corresponding Federal Match	-	86	86	62	38	272
Reduce Number of 330s as IPAs Under Mi Salud	-	5	5	5	5	20
Create the Puerto Rico Medical Center Campus	(2)	10	19	19	19	65
Control Health Care Costs	**(4)**	**151**	**179**	**155**	**131**	**612**
Total Expense Measures	**$11**	**$443**	**$1,064**	**$1,538**	**$1,859**	**$4,914**

Summary of Measures – Growth, Costs and Total Impact

A summary of the annual impact of the incremental revenue from GNP growth, which is spurred by economic development and structural reforms as determined by the Working Group, is presented below along with a summary of the estimated cost of implementing all of the measures and then the total impact of the growth and measures

- Consistent with the approach taken in the Krueger Report, incremental revenue from economic development and structural reforms is calculated as the difference between a high-growth and a base-case scenario for General Fund revenue sources(1)

- The base-case scenario assumes approximately -1% real growth in GNP while the high-growth scenario assumes structural reforms lead to GNP growth of 2% by 2020 (2% inflation is assumed in both cases)
  - In addition, labor reforms are assumed to lead to a greater increase in revenues from personal income taxes, which is calculated using an elasticity factor of 1%, which is also consistent with the Krueger Report

- Incremental costs of the various measures are also shown below and consist of estimates of incremental capex necessary for the measures and growth, incremental pension contributions associated with the measures, cost of earned income tax credits, investment in a new accounting system and the implementation of a new Institute of Statistics plan

$ millions	2016P	2017P	2018P	2019P	2020P	Total
Total Est. Incremental Rev. from Econ. Dev. and Structural Reforms	**–**	**$115**	**$322**	**$584**	**$907**	**$1,929**
Estimated Incremental Cost of Measures	**($262)**	**($549)**	**($569)**	**($616)**	**($538)**	**($2,533)**
Total Impact of Measures						
Revenue Measures	1,121	1,375	1,943	2,506	2,524	9,469
Expense Measures	11	443	1,064	1,538	1,859	4,914
Incremental Cost of Measures	(262)	(549)	(569)	(616)	(538)	(2,533)
Total Impact of Measures	**$870**	**$1,269**	**$2,439**	**$3,428**	**$3,845**	**$11,850**
Est. Incremental Rev. from Economic Development and Structural Reforms	–	115	322	584	907	1,929
Total Impact of Measures and Growth	**$870**	**$1,384**	**$2,761**	**$4,012**	**$4,752**	**$13,779**

(1) General Fund revenue sources include personal income, corporate, SUT/VAT, property, Act 154, alcoholic beverages, cigarettes, motor vehicles, excises on off-shore shipment rum and other taxes. Act 154 taxes are assumed to be held constant in both base- and high-growth scenarios.

Working Group for the Fiscal and Economic Recovery of Puerto Rico

Summary of Fiscal Responsibility and Economic Revitalization Act

Fiscal Responsibility and Economic Revitalization Act

In order to ensure maximum benefit from the FEGP, the Working Group has drafted the Fiscal Responsibility and Economic Revitalization Act (FRERA) that includes measures that will ensure compliance with the FEGP, including the creation of a control board (and other oversight and compliance measures) as well as new budgetary rules

Selected Highlights of FRERA: The Control Board (or the "Board") Generally

- Establishes the Board, which will consist of five individuals appointed by the Governor that must have knowledge and expertise in finance, management, or the operation of business or government and must be independent from other governmental entities
- Provides that Board members will serve for 4-year staggered terms
- Requires that a majority of the nominated Board members be selected from a list provided to the Governor by independent third parties
- Gives the Board oversight authority over most governmental entities, including the Commonwealth, GDB and the public corporations (except PREPA and PRASA)
- Assures the Board's independence by
  - Giving it its own revenue source for operations
  - Allowing it to hire its own independent staff and professionals
  - Removing a board member only for cause
  - Giving it extensive subpoena powers
  - Authorizing it to levy sanctions for non-compliance with approved budgets

Fiscal Responsibility and Economic Revitalization Act

Selected Highlights of FRERA: Fiscal and Economic Growth Program

- Requires that a Commonwealth-wide consolidated 5-year FEGP be submitted to the Board for approval no later than the end of the 2nd Quarter of FY 2016
- Requires the Board to evaluate whether the proposed FEGP complies with the objectives and requirements provided in the FRERA
- Mandates that the objectives of the FEGP include:
  - Implementing structural reforms that restore economic growth and competitiveness
  - Eliminating, over time, the financing gaps and reducing the debt burden of most governmental entities, including the Commonwealth and public corporations (except PREPA and PRASA)
  - Improving institutional credibility by improving budget formulation and execution and data transparency

Fiscal Responsibility and Economic Revitalization Act

Selected Highlights of FRERA: FEGP (cont.)

- Requires the FEGP to:
  - Include specific proposals to improve and diversify the economy
  - Incorporate structural and economic reforms to ensure long-term fiscal sustainability and economic development
  - Incorporate best practices for making reliable revenue estimates
  - Require that budgets be prepared and calculated pursuant to the modified accrual basis of accounting according to generally accepted standards
  - Require governmental entities to reduce annually, and by FY 2021, eliminate budget deficits
  - Ensure a material reduction in expenditures through more efficient delivery of services
  - Ensure that pension obligations are sustainable and can be honored over the long term
  - Require that the Commonwealth-wide debt load be adjusted to sustainable terms
  - Require that financial controls and accounting systems be improved to monitor fiscal developments on a timely basis
  - Identify automatic budgetary stabilizers to ensure compliance with the proposed FEGP

Fiscal Responsibility and Economic Revitalization Act

Selected Highlights of FRERA: Approval of, and Monitoring Compliance with, the FEGP

- Requires the Board to review and approve the consolidated Fiscal and Economic Growth Plan if it complies with the objectives and requirements set forth in FRERA
- Requires certain entities to submit annual budgets to the Board to ensure that they comply with the approved Fiscal and Economic Growth Plan
- Requires the Board to evaluate whether the budgets comply with the Fiscal and Economic Growth Plan
- Requires the Board to issue non-compliance findings if the budgets do not comply with the Fiscal and Economic Growth Plan
- Requires the Board to monitor compliance with the approved budgets throughout each fiscal year
- Requires the Board to issue non-compliance warnings during the fiscal year or findings at the end of the fiscal year if the entities' actual revenues and expenditures vary from the approved budget in an amount that exceeds a permitted variance determined by the Board
- Imposes severe sanctions for failing to comply with approved budgets, which may include:
  - A prohibition on entering into contracts
  - Automatic hiring freezes
  - Automatic expense cuts (see next slide)

Fiscal Responsibility and Economic Revitalization Act

Selected Highlights of FRERA: New Budgetary Rules for the Commonwealth General Fund

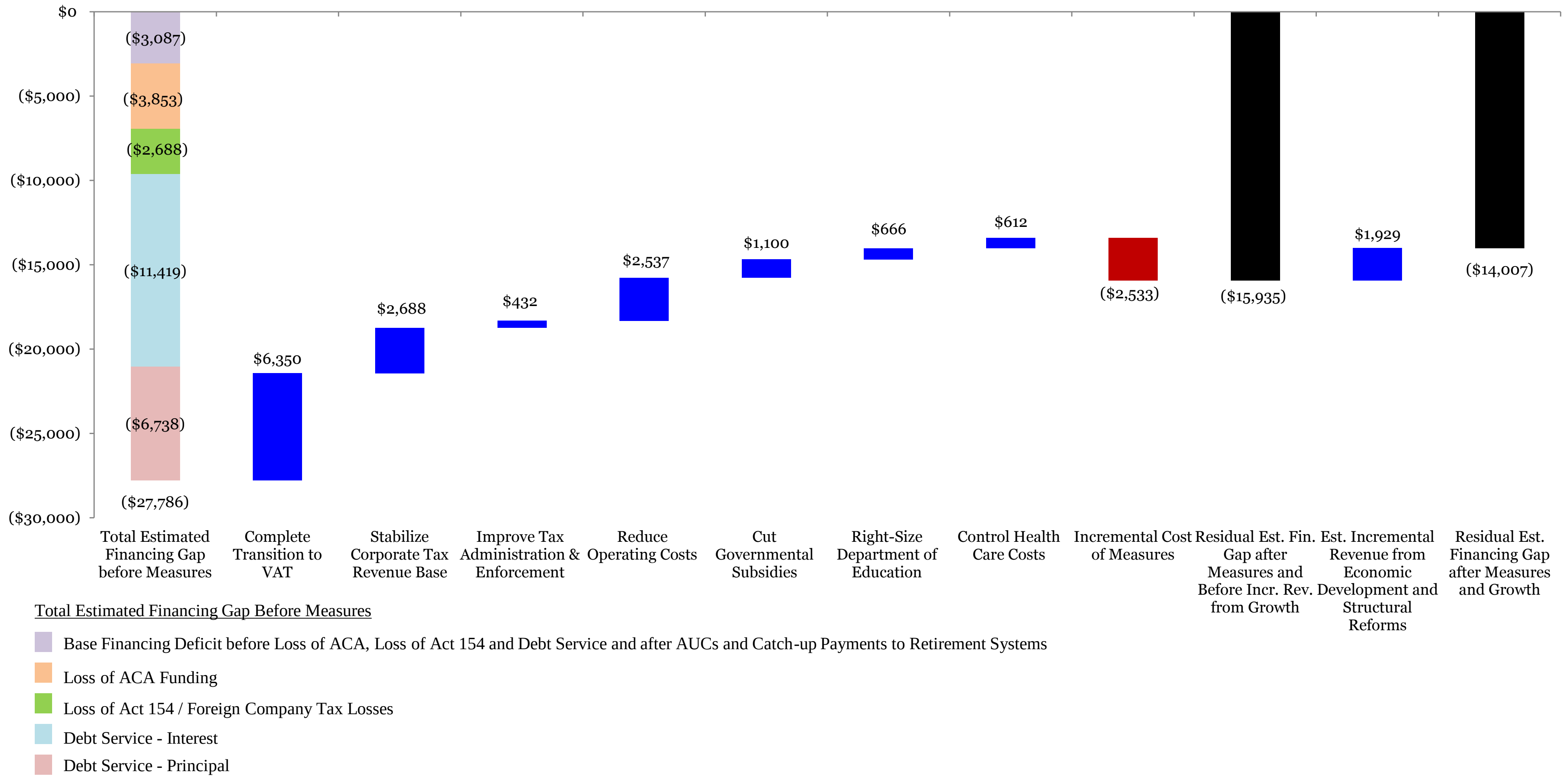
- Provides that the Commonwealth budget be based on a "Revenue Projection" validated by third parties
- Requires that the budget include a 5-year revenue and expense projection
- Prohibits the creation or use of budgetary funds without an identified source of revenues and cancels several existing budgetary funds that do not have identified sources of revenues
- All purchase orders and contracts with third-party suppliers will be subject to OMB budgetary oversight and uniform procedures for approval and recording
- Creates a special fund that may only be used to pay the government's accounts payable, including tax refunds; amounts to be deposited in such fund shall not be included in the Revenue Projection
- Provides that the Secretary of the Treasury shall adjust each fiscal year's actual revenue numbers by the difference between the projection of tax refunds made at the beginning of the fiscal year and the revised projections of tax refunds made near the end of the fiscal year
- Provides that a specified amount of each fiscal year's budget be allocated to a "Budgetary Reserve Fund" until amounts credited to such fund reach a specified percentage of the then-current fiscal year's Revenue Projection
- Provides that budgetary expenditures for each fiscal year cannot exceed such fiscal year's Revenue Projection less the amount allocated to the "Budgetary Reserve Fund" amount
- Provides that the Budgetary Reserve Fund may only be used for certain specified purposes
- Mandates that the budget identify a specified amount of operating expenditures that may not be incurred unless OMB (and in some cases the Board) authorizes the use of such funds (known as the "Sequestered Expenditures")
- Provides that a portion of the Sequestered Expenditures shall be released by the OMB or the Board at the end of each fiscal quarter if actual revenues meet or exceed the Revenue Projection
- Provides that if actual revenues are below the Revenue Projection, the Sequestered Expenditures shall not be released
- Provides that the OMB or the Board may also decide not to release the Sequestered Expenditures to specific entities if it determines that such entities' actual expenditures will exceed its budgeted expenditures

Summary of Projected Financing Gap After Measures

Cumulative Financing Gap Before and After Measures

A summary of the cumulative financing gap before measures from FYs 2016 to 2020[(1)] and the total benefit from each measure over the same period, as determined by the Working Group, is shown below

Cumulative 5-Year Financing Gap ($ millions)



(1) Note that the financing gap before measures has been updated from the Krueger Report, based on new information obtained through diligence by the Working Group. The variances to the Krueger Report are detailed in the appendix.

Annual Financing Surplus (Gap) Before Debt Service

Based on the Working Group's diligence and the measures previously outlined, the following presents a summary of the estimated annual financing gaps prior to the payment of debt service, but after the implementation of the measures previously outlined

Projected Financing Surplus/(Gap) before Debt Service ($ millions)

	2016P	2017P	2018P	2019P	2020P	Total
Total Estimated Financing Gap before Measures (incl. Debt Service)	($4,075)	($4,386)	($4,670)	($7,437)	($7,217)	($27,786)
Consolidated Interest	2,320	2,370	2,320	2,239	2,170	11,419
Consolidated Principal	1,810	1,044	957	1,628	1,299	6,738
Pre-Measures & Pre-debt Service Financing Surplus/(Gap)	55	(972)	(1,392)	(3,571)	(3,749)	(9,628)
Revenue Measures						
Complete Transition to VAT	1,111	1,290	1,303	1,316	1,330	6,350
Stabilize Corporate Tax Revenue Base	–	–	538	1,075	1,075	2,688
Improve Tax Administration & Enforcement	10	85	103	115	119	432
Total Revenue Measures	1,121	1,375	1,943	2,506	2,524	9,469
Expense Measures						
Reduce Operating Costs	3	165	550	840	979	2,537
Cut Governmental Subsidies	–	50	200	350	500	1,100
Right-Size Department of Education	12	78	135	193	249	666
Control Health Care Costs	(4)	151	179	155	131	612
Total Expense Measures	11	443	1,064	1,538	1,859	4,914
Incremental Cost of Measures(1)	(262)	(549)	(569)	(616)	(538)	(2,533)
Fin. Surplus before Debt Serv. ex. Economic Growth	**$924**	**$298**	**$1,046**	**($143)**	**$97**	**$2,222**
Est. Incremental Revenue from Economic Development and Structural Reforms	–	115	322	584	907	1,929
Financing Surplus before Debt Service	**$924**	**$413**	**$1,369**	**$442**	**$1,003**	**$4,150**

(1) Includes estimates of incremental capex necessary for the measures and growth, incremental pension contributions associated with the measures, cost of earned income tax credits, investment in a new accounting system and the implementation of a new Institute of Statistics plan.

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Unsustainability of Existing Debt Service Absent Economic Growth

Even after taking the measures outlined on the previous pages, the FEGP suggests that the Commonwealth cannot service all of its debt as currently scheduled

- Since economic growth is dependent in many ways on elements outside of the Commonwealth's control (such as changes to certain federal government policies), the following exhibit presents the forecasted financing gaps after debt service excluding the estimated impact of GNP growth from economic development and structural reforms
- The financing gap below is shown for illustrative purposes only based on consolidated debt service and with GO bond and GO guaranteed bond debt service(1) separately delineated

Total Projected Financing Surplus/(Gap) Excluding Economic Growth ($ millions)

	2016P	2017P	2018P	2019P	2020P	Total
Financing Gaps Based on Consolidated Interest and Principal						
Fin. Surplus before Debt Serv. and Est. Incr. Rev. from Econ Dev. And Struct. Reforms	$924	$298	$1,046	($143)	$97	$2,222
Consolidated Interest(2)	(2,320)	(2,370)	(2,320)	(2,239)	(2,170)	(11,419)
Financing Gap after Consolidated Interest	(1,396)	(2,073)	(1,274)	(2,382)	(2,073)	(9,197)
Consolidated Principal(2)	(1,810)	(1,044)	(957)	(1,628)	(1,299)	(6,738)
Total Financing Gap before Economic Growth	**($3,205)**	**($3,117)**	**($2,231)**	**($4,010)**	**($3,372)**	**($15,935)**
Financing Gaps with GO and GO Guaranteed Debt Service Delineated						
Fin. Surplus before Debt Serv. and Est. Incr. Rev. from Econ Dev. And Struct. Reforms	$924	$298	$1,046	($143)	$97	$2,222
GO and GO Guaranteed Interest(1)	(920)	(953)	(932)	(895)	(860)	(4,561)
GO and GO Guaranteed Principal(1)	(925)	(526)	(433)	(483)	(553)	(2,920)
Financing Surplus after GO and GO Guaranteed Debt Service	(921)	(1,182)	(319)	(1,521)	(1,317)	(5,259)
Interest Excluding GO and GO Guaranteed	(1,400)	(1,418)	(1,387)	(1,345)	(1,309)	(6,859)
Financing Gap after GO and GO Guaranteed and All Interest	(2,320)	(2,599)	(1,707)	(2,865)	(2,626)	(12,118)
Principal excluding GO and GO Guaranteed	(885)	(518)	(524)	(1,144)	(746)	(3,818)
Total Financing Gap before Economic Growth	**($3,205)**	**($3,117)**	**($2,231)**	**($4,010)**	**($3,372)**	**($15,935)**

(1) GO and GO guaranteed debt service includes debt service payments related to GO, GDB GO guaranteed bonds, PBA and PRIFA Bond Anticipation Notes ("BANs"). Excludes PRASA and GDB guaranteed intragovernmental loans.
(2) Includes any debt service payments related to debt at GO, GDB, PBA, Public Finance Corporation ("PFC"), COFINA, PRIFA, UPR, Puerto Rico Convention Center District Authority ("PRCCDA"), Puerto Rico Industrial Development Company ("PRIDCO"), GSA, PRIFA BANs, ERS and HTA.

Unsustainability of Existing Debt Service Even with Economic Growth

Even if the Commonwealth were able to achieve economic growth, the estimated benefit of such growth still would not be enough to allow the Commonwealth to pay all of its contractual debt service as currently scheduled

- The financing gap presented below is shown after the estimated benefit of economic growth; as with the previous page, the financing gap is shown based on consolidated debt service and with GO bond and GO guaranteed bond debt service[1] separately delineated

Total Projected Financing Surplus/(Gap) Including Economic Growth ($ millions)

	2016P	2017P	2018P	2019P	2020P	Total
Financing Gaps Based on Consolidated Interest and Principal						
Financing Surplus before Debt Service	$924	$413	$1,369	$442	$1,003	$4,150
Consolidated Interest[2]	(2,320)	(2,370)	(2,320)	(2,239)	(2,170)	(11,419)
Financing Gap after Consolidated Interest	(1,396)	(1,958)	(951)	(1,798)	(1,166)	(7,269)
Consolidated Principal[2]	(1,810)	(1,044)	(957)	(1,628)	(1,299)	(6,738)
Total Financing Gap	**($3,205)**	**($3,002)**	**($1,909)**	**($3,425)**	**($2,465)**	**($14,007)**
Financing Gaps with GO and GO Guaranteed Debt Service Delineated						
Financing Surplus before Debt Service	$924	$413	$1,369	$442	$1,003	$4,150
GO and GO Guaranteed Interest[1]	(920)	(953)	(932)	(895)	(860)	(4,561)
GO and GO Guaranteed Principal[1]	(925)	(526)	(433)	(483)	(553)	(2,920)
Financing Surplus after GO and GO Guaranteed Debt Service	(921)	(1,067)	3	(936)	(410)	(3,331)
Interest Excluding GO and GO Guaranteed	(1,400)	(1,418)	(1,387)	(1,345)	(1,309)	(6,859)
Financing Gap after GO and GO Guaranteed and All Interest	(2,320)	(2,484)	(1,385)	(2,281)	(1,719)	(10,189)
Principal excluding GO and GO Guaranteed	(885)	(518)	(524)	(1,144)	(746)	(3,818)
Total Financing Gap	**($3,205)**	**($3,002)**	**($1,909)**	**($3,425)**	**($2,465)**	**($14,007)**
Memo: Total Financing Gap ex. Est. Incremental Revenue from Economic Development and Structural Reforms	*($3,205)*	*($3,117)*	*($2,231)*	*($4,010)*	*($3,372)*	*($15,935)*

(1) GO and GO guaranteed debt service includes debt service payments related to GO, GDB GO guaranteed bonds, PBA and PRIFA BANs. Excludes PRASA and GDB guaranteed intragovernmental loans.
(2) Includes any debt service payments related to debt at GO, GDB, PBA, PFC, COFINA, PRIFA, UPR, PRCCDA, PRIDCO, GSA, PRIFA BANs, ERS and HTA.

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Conclusion

Conclusion

- Even after the implementation of the FEGP, which is subject to significant political and execution risks, the Working Group's projections suggest that the Commonwealth cannot meet all of its debt service requirements as currently scheduled and must restructure its liabilities. Further, without significant changes in federal policies, particularly in health care and economic development, the ability of the Commonwealth to meet its debt service costs while providing essential services to its residents will be severely challenged
- While the Working Group recognizes that a restructuring of the Commonwealth's debt would result in hardship to individual bondholders, the Working Group believes that, unless the persistent stagnation of Puerto Rico's economy that has helped fuel the increase in Government debt over the past decade can be reversed, the public debt is not sustainable
- Therefore, in order to make the greatest amount of the debt sustainable in the long term, priority has to be given to:
  - Reigniting Puerto Rico's economic growth in the short- and medium-term;
  - Providing essential services, including health, education and safety, to the people of Puerto Rico, the continued deterioration of which will exacerbate the Commonwealth's negative demographic trends, adversely affect its economic prospects and erode its tax base; and
  - Ensuring government can sustain its pension obligations
- The Fiscal and Economic Growth Plan was designed with these priorities in mind

Conclusion (cont.)

- As difficult as debt restructuring is likely to be, the Working Group has instructed its advisors to begin working on a voluntary exchange offer to be made to its creditors as part of the implementation of the Fiscal and Economic Growth Plan
- In the design of the voluntary exchange offer, the Working Group has directed its advisors to take into account the priority accorded to various debt instruments across the Puerto Rico debt complex, including its GO debt, while recognizing that, even assuming the clawback of revenues supporting certain Commonwealth tax-supported debt, available resources may be insufficient to service all principal and interest on debt that has a constitutional priority
- Therefore, a consensual compromise of the creditors' competing claims to the Commonwealth's revenues to support debt service will be required in order to avoid a destabilizing default on the Commonwealth's debt and to avoid a legal morass that will further destabilize the Commonwealth's economy and finances
- Accordingly, the Working Group has directed its advisors to meet with the creditor groups that have already been organized (and those that may be formed hereafter) to explain the Fiscal and Economic Growth Plan and to begin negotiation of the terms of a voluntary exchange offer that can garner widespread creditor acceptance
- **It is the Working Group's belief that a voluntary adjustment of the terms of the Commonwealth's debt that allows the measures contained in the FEGP to be implemented is the best way to maximize all creditor recoveries**

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Appendix

Bridge from Budget to Conway

Risk Adjustments to FY 2016 Budget

- The FY 2016 general fund budget, which is included in the CM TSA adjusted cash flow was adjusted for the potential risks below:
  - Revenue risk shortfall of $306.4 million is primarily attributable to unfavorable revenue variances for May 2015 and June 2015
  - Litigation settlement of $5.1 million (not included in the FY 2016 budget related to the Dept. of Health)
  - Debt risk of $402.0 million is primarily related to debt obligations owed to GDB, for bonds held in the GDB portfolio, and debt service payments related to the Puerto Rico Public Finance Corporation, as follows:
    - $308.3 million – contractually obligated debt payments for FY 2016 related to obligations owed to GDB. These debt service payments were not approved by the Legislative Assembly in the FY 2016 budget. Payment of this debt on terms other than the contractual terms could have a negative impact on GDB's liquidity and its ability to pay obligations as they become due
    - $93.7 million – the Legislative Assembly may appropriate for PFC debt service in FY 2016
  - A proposed Economic Development and Obligations Payment Fund totaling $275.0 million has been created to be used for economic development initiatives and/or the payment of obligations pending legislative approval

Risk Adjustment to General Fund Budget ($ millions)

	FY 2016
Revenue	($306)
Litigation settlement	(5)
Debt	(402)
Economic Development & Obligations Payment Fund	275
Budget Adjustments	**($439)**

Source: Commonwealth of Puerto Rico Liquidity Update – Conway MacKenzie, Aug. 25, 2015.

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Bridge from Conway to the Krueger Report

Reconciliation of Conway and Krueger Reports

- The Krueger Report measured a deficit under an approach that is different than Conway's approach in the following areas: the Krueger Report generally used an accrual accounting method as compared to cash; the Krueger Report's methodology included GDB debt owed to third-parties versus Conway's approach that included debt obligations owed to GDB; and finally, the Krueger Report's scope included the broader Commonwealth financial position and Conway's approach only includes inflows and outflows of the TSA account as noted below:
  - FY 2016 General Fund budget
  - Federal funds
  - Net pension benefits
  - Non-General Fund revenue/expenses through the TSA
  - CM Risk Adjustments to the TSA (debt, working capital, etc.)
  - Commonwealth's Liquidity Enhancement Measures
  - Select Component Units (ASES, PRITA, UPR, PBA, ASEM)
  - CM's analysis does not include cash flow projections for the following:
    - Component Units, aside from the five noted above
    - Non-General Fund governmental funds
    - Special revenue funds
    - Special debt funds
    - Capital project funds
    - Non-major proprietary funds
    - Other non-governmental and fiduciary funds
    - Municipalities and the Municipal Property Tax Collection Center ("CRIM")
  - Conway's analysis does not include cash flow projections for the following:
    - Litigation risk
    - Budget adjustment risk – reduction in spending from FY 2015 to FY 2016
    - Spending in excess of appropriations
    - Federal funding risk
    - Unfavorable economic factors
    - Extraordinary expenses associated with any restructuring activities

Conway to Krueger Report Bridge ($ millions)

	CM Adj. TSA CF	Liq. Outlook	FY2016
Krueger Deficit (after revenue measures)	($2,518)	–	($2,518)
Tax and Non-Tax Variance	(73)	150	77
GDB Net Operating Revenue	(130)	–	(130)
Other Fund Inflows	36	–	36
Total Inflows(1)	**(167)**	**150**	**(17)**
General Fund Budget	143	(183)	(41)
Net Op. Deficit of Non-GF Gov. Funds	362	–	362
Net Op. Deficit of Non-Enterprise Comp. Units	350	(193)	157
Capital Expenditures	300	–	300
Due to Intragovernmental	–	(500)	(500)
FY2015 Deferred Appropriations (Ex. Debt)	(124)	–	(124)
Non-debt Related Outflows(1)	**1,031**	**(876)**	**155**
Budgeted Debt + Debt Outflows	230	(150)	80
Other Debt	523	–	523
Total Debt(2)	**754**	**(150)**	**603**
Working Capital	(438)	400	(38)
Revenue Measures, Net of VAT	**63**	**–**	**63**
Total Variance	**$1,992**	**($1,277)**	**$716**
CM Liquidity Outlook (3)	**($525)**	**($1,277)**	**($1,802)**

Source: Krueger Report

Note: Terms defined herein are referenced in more detail within Conway MacKenzie's Liquidity Update of the Commonwealth of Puerto Rico (Aug. 25, 2015).
(1) Variance of inflows and outflows are net of Federal Funds which have a net zero impact. Krueger reports $6.5 billion where CM's TSA cash flow includes $3.0 billion.
(2) GDB debt variances totaling $570 million are related to a different approach in debt disbursements. CM's report includes debt due to GDB, the Krueger Report includes debt owed to third-parties.
(3) The bank to book reconciliation as of June 30, 2015 was approximately $442.6 million. This risk is not included in the reconciliation above, but is noted in Conway's report.

Adjustments to the Krueger Report

As part of its development of the FEGP, the Working Group reviewed not only the reform measures identified in the Krueger Report, but also the estimates in the Krueger Report for the Commonwealth's financing gaps before the impact of the measures

- The Working Group's estimate of the total financing gaps facing the Commonwealth generally followed the approach outlined in the Krueger Report
- However, a review of the basis for many of the estimates in the Krueger Report resulted in numerous changes, including:
  - Revised revenue forecasts that incorporated actual results for 2015 that were not available to the Krueger team at the time its report was issued
  - More detailed component unit projections developed by Conway MacKenzie after the release of the Krueger Report
  - Revised capital expenditure estimates on a by-project rather than simply based on historical numbers as was done in the Krueger Report
  - Revised budgetary expense projections from OMB as well as the adjustment of an overestimation of certain expenses (and the resulting impact of Law 66 on these expenses) included in the Krueger Report
    - The revised OMB projections included revised estimates of required additional uniform pension contributions that in turn impacted the estimated shortfalls in the retirement funds that were included in the Krueger Report

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Adjustments to the Krueger Report (cont.)

- In addition, the decision was made to incorporate HTA into the projections, unlike in the Krueger Report
  - Excluding federal grants, the majority of HTA's revenues come from gas and petroleum taxes collected by the Commonwealth
  - In addition, HTA has been funded with over $2 billion of loans from GDB
  - Based on these factors, it was determined that HTA should be included in the model to capture a holistic view of Commonwealth-supported entities and resulting deficits on a consolidated basis, as was the goal of the methodology outlined in the Krueger Report
- These changes, the Adjusted Estimates, were reviewed with, and reflect the input of, members of the Krueger team
- The following pages provide a summary bridge from the Krueger Report to the Adjusted Estimates (the consolidated adjusted estimates are also presented earlier in the presentation)

Bridge from Krueger to Adjusted Estimates

The following exhibit presents a summary of the variances between the Krueger Report and the Adjusted Estimates (prior to the implementation of any measures)

Bridge from Krueger Report to Adjusted Estimates ($ millions)

	2016P	2017P	2018P	2019P	2020P	Comments
Krueger Report Fin. Gap Bef. Measures	**($3,676)**	**($4,169)**	**($5,893)**	**($7,028)**	**($7,147)**	
Variances in Adjusted Estimates						
General Fund and Other Select Revenues	(83)	(152)	(194)	(236)	(279)	Revised revenue estimates that incorporate preliminary actual 2015 results that were lower than what had been estimated in the Krueger Report; 2015 revenues form the base for future year estimates. Comparison shown is against the sum of Krueger Report tax and non-tax revenues
GDB Net Operating Revenue (including PRIFA crudita receipts and PRIFA Petroleum Receipts)	(385)	(287)	(82)	(45)	(84)	Revised forecast from GDB. Note that the differential is shown after a deduction of PRIFA BAN debt service (which, in the Adjusted Estimates, is shown in the debt service line, whereas in the Krueger Report it was embedded in the GDB Operating Revenue line). Adjusted Estimates do not include any new loans to the municipalities, only funding on existing lines
COFINA SUT Collection	15	15	16	16	16	Revised forecast based on revised revenue estimates and the development of a waterfall model that projects the SUT allocations; the Krueger Report set COFINA revenues equal to COFINA debt service

Bridge from Krueger to Adjusted Estimates (cont.)

Bridge from Krueger Report to Adjusted Estimates ($ millions)

	2016P	2017P	2018P	2019P	2020P	Comments
HTA Operating Income and Debt Service (ex. Capex)	75	124	172	191	191	HTA is included in the Adjusted Estimates but was excluded from the Krueger Report; numbers here are shown inclusive of all revenues, expenditures (ex. capital expenditures shown in the capital expenditures variance line) and debt service
GF budget (ex. Debt Service and Additional Uniform Contributions)	(102)	(280)	(75)	74	169	Revised budget per OMB as well as adjustment of an overestimation contained in the Krueger Report of certain expenses (and the resulting impact of Law 66 on these expenses). Adjusted Estimates exclude additional uniform contributions for illustrative purposes, whereas the Krueger Report had included the additional uniform contributions in this line (though at a lower amount than included in the most recent OMB projections). In the Adjusted Estimates, ERS debt service was also deducted from the ERS appropriations embedded in the General Fund budget from OMB and then included in the principal and interest lines; the Krueger Report embedded ERS debt service in the retirement shortfall

Bridge from Krueger to Adjusted Estimates (cont.)

Bridge from Krueger Report to Adjusted Estimates ($ millions)

	2016P	2017P	2018P	2019P	2020P	Comments
Additional Uniform Contributions as Compared to Retirement Shortfall	(194)	88	458	(78)	70	Adjusted Estimates run through higher additional uniform contributions, which reduce the "Retirement Shortfall"; the comparison shown here represents the Additional Uniform Contribution in the Adjusted Estimates (including certain catch-up payments) as compared to the Retirement Shortfall shown for each year in the Krueger Report as well as the AUC embedded in the Krueger Report "GF Budget" line. Adjusted Estimates exclude $58 million annually of estimated AUCs required by municipalities that have historically relied on limited GDB liquidity to fund
Non-General Fund Government Funds	127	129	130	131	132	Represents revised estimates of "non-budgeted funds." Excludes any losses from agencies with independent treasuries, which were included in the Krueger Report, based on further diligence and the inclusion of such outflows in other lines (namely, capex)
Component Units ex. Capex	230	413	256	552	687	Updated for detailed component unit projections that were not available at the time of the Krueger Report
Capital Expenditures	(86)	(285)	(245)	(203)	(38)	Krueger Report based on most recent historical estimates. Adjusted Estimates based on actual schedule of projects not available at the time of the Krueger Report. Adjusted Estimates do not include municipal capital expenditures, which have historically been largely funded by the Commonwealth and GDB

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Bridge from Krueger to Adjusted Estimates (cont.)

Bridge from Krueger Report to Adjusted Estimates ($ millions)

	2016P	2017P	2018P	2019P	2020P	Comments
Change in Payables	450	(377)	(51)	(51)	(51)	Krueger Report had made a blanket assumption of a constant reduction in payables; Adjusted Estimates include a more detailed analysis that reduces payables to ~35 days payable outstanding, assumes different repayment periods for different types of payables (i.e., tax refunds are paid on an accelerated schedule as compared to certain other payables), and that the repayment of payables does not begin until FY 2017
Change in Deposits and Deposit Replenishment	(551)	(500)	–	–	–	Based on updated deposit balance information that was not available at the time of the Krueger Report; Amount required for GDB to meet its estimated minimum statutory liquidity requirement of $350 million and the Commonwealth to have $1.0 billion of total deposits on hand by FY 2016 and $1.5 billion by FY 2017
Inflows from Other Entities	105	–	–	–	–	Represents identified inflows from entities outside the model used to cover expenses in the FY 2016 budget
Loss of ACA Funding	–	–	474	(597)	(730)	Updated per revised estimates based on further diligence done on ASES that was not available at the time of the Krueger Report
Act 154 / Foreign Company Tax Losses	–	894	365	(163)	(154)	Updated based on revised diligence conducted with PRIDCO. The impact of the loss of Act 154 is not assumed to begin until halfway through FY 2018
Total Variances in Adjusted Estimates	($399)	($217)	$1,224	($409)	($70)	
Adjusted Estimates before Measures	**($4,075)**	**($4,386)**	**($4,670)**	**($7,437)**	**($7,217)**	

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Total Public Sector Debt

The following summarizes total public sector debt as of June 30, 2015

Total Public Sector Debt Outstanding ($ millions)

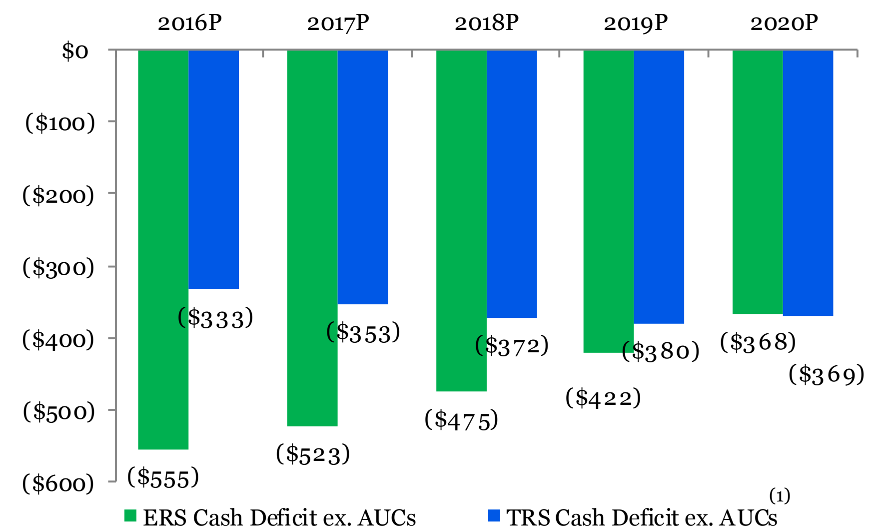
	6/30/15
Full Faith and Credit Bonds and Notes Issued by the Commonwealth	$13,061
Bonds and Notes Guaranteed by the Commonwealth	5,547
Subtotal	**18,608**
Debt Supported by Commonwealth Appropriations or Taxes	4,047
Tax and Revenue Anticipation Notes	300
Subtotal - Debt Payable from the General Fund	**22,955**
Bonds and Notes Payable from Sales and Use Tax Revenue (COFINA)	15,224
Debt Issued by Public Corporations and Other Instrumentalities	23,877
Debt Issued by Municipalities	4,126
Pension Funding Bonds (Payable from Employer Contributions to ERS)	2,948
Other Limited Obligations Debt and Non-recourse Debt	1,987
Subtotal - Other Public Sector Debt	**48,162**
Total Public Sector Debt	**$71,117**

Note: Not all entities included in the chart above are included in the Adjusted Estimates, consistent with the Krueger Report.

Retirement Systems Assumptions, Asset Balances and Cash Flows

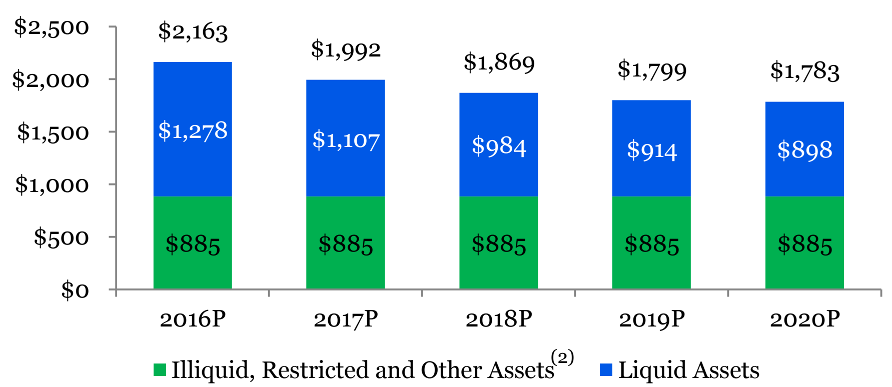
- The following charts summarize the declining asset portfolios of the retirement plans and certain assumptions embedded therein for purposes of developing the FEGP
- Key baseline assumptions include:
  - ERS: ~2% payroll growth starting in FY 2018, begin to receive AUCs of $352 mm in FY16, assuming the receipt of past-due contributions from the General Fund, municipalities and public corporations
  - TRS: ~2% payroll growth starting in FY 2018, begin to receive AUCs of $30 mm in FY17 & 18 and $510mm from FY19 forward
  - JRS: Modeled per June 30, 2014 actuarial valuation cash flows; projected ending balance in FY 2016 of ~$30 mm expected to be depleted by FY 2018, after which it is assumed that General Fund employs "pay-go" funding of ~$20 mm per year
- In a scenario that includes accelerated attrition, each retirement plan's stock of assets would decline faster, necessitating larger AUCs from the central government
- Failure of municipalities or agencies to make contributions would exacerbate asset declines; historically, agencies and municipalities have relied on, among other sources, short-term financing from GDB and others to make such payments and that funding source may not be available going forward

ERS and TRS Yearly Cash Deficits Ex. AUC ($ millions)

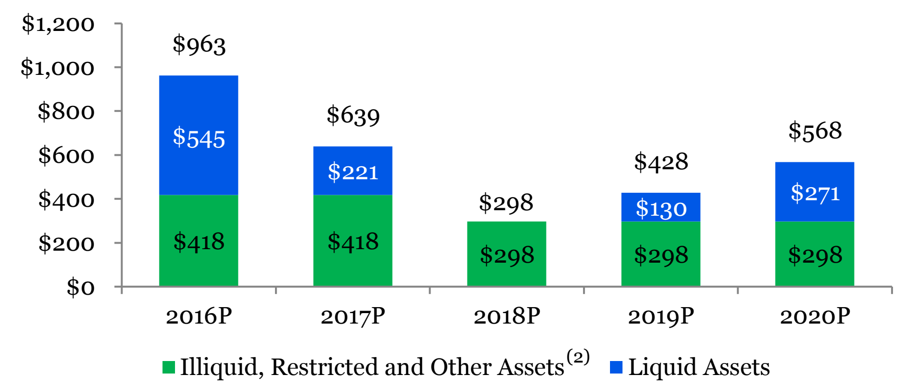


	2016P	2017P	2018P	2019P	2020P
ERS AUCs	$428	$352	$352	$352	$352
TRS AUCs	–	$30	$30	$510	$510

ERS Ending Asset Balance ($ millions)



TRS Ending Asset Balance ($ millions)(1)



Note : All data sourced by preliminary data from the actuarial firm's valuation reports and incorporating certain assumptions from ERS, TRS and GDB. All figures are preliminary in nature and subject to substantial revision pending a complete review of the retirement plans by the actuarial firm based on the latest available actual figures. Many factors affecting the pension are outside their control including actual performance of asset portfolios, plan participant attrition rates, general fund budgeting and policy decisions. These projections may not adhere to GASB accounting. None of the actuarial firm, ERS, TRS or GDB conducted a comprehensive evaluation of these projections and none of the aforementioned parties makes any representation or warranty, express or implied, as to the accuracy or completeness of the assumptions herein.

(1) Projections based valuation as of June 30, 2014, and not updated for FY 2015 performance. Important to note that actual payroll benefit payments were ~$100 mm higher in FY 2015 and projected to be ~$120 mm higher in FY 2016 than the baseline projection from the latest actuarial valuation. Potentially, this trend could continue, which could, in turn, lead to a higher AUC estimate for TRS once the June 30, 2015 valuation is performed.

(2) Illiquid, Restricted and Other Assets includes restricted cash, unrestricted cash at GDB and COFINA investments, net of accrued liabilities.

Footnotes for Financing Gaps Before Measures (p. 17)

1. General Fund and Other Select Revenues include General Fund revenues as well as transfers from the Municipal Revenues Collection Center (known as “CRIM”) and hotel tax revenues received by PRCCDA, consistent with the Krueger Report. Revenue estimates were revised to reflect greater knowledge of actual collections in 2015 as well as additional diligence done on certain tax revenues, in particular, those associated with the sales and use tax (“SUT”) and the foreign entity tax (Act 154).
2. GDB net operating revenue includes net cash flows from its loan portfolio to entities outside of the scope of the Adjusted Estimates as well as PRIFA petroleum tax receipts (which provide an average of $310 million per year over the projection period). The Krueger Report had netted payments on account of the PRIFA BANs, but in the Adjusted Estimates the debt service associated with the PRIFA BANs is included in the interest and principal lines. Estimates were also revised by GDB. Projections do not include any new loans to the municipalities, only funding on existing lines.
3. COFINA revenues were estimated using a SUT tax waterfall based on current policies and information developed by the Commonwealth. The revenues shown each year correspond to the Pledged Sales Tax Base Amount as defined in the COFINA bond documents. The Krueger Report had set COFINA revenues equal to COFINA debt service.
4. Unadjusted since the Krueger Report.
5. HTA revenues include gas taxes, license fees, toll receipts, investments, petroleum taxes, cigarette taxes, Tren Urbano related receipts for FY2016, and other highway and operating receipts. The HTA projections assume the Tren Urbano is transferred to PRITA in FY 2017.
6. Based on revised estimates of the budget from OMB. Excludes identified additional uniform contributions and debt service. Also adjusts appropriations to PBA and UPR to deduct debt service (which is then included in the principal and interest lines shown separately, similar to the Krueger Report).
7. Additional uniform contributions related to General Fund payments to fund the retirement systems and certain catch-up payments related to unpaid AUC amounts in FY 2014 and FY 2015. Also includes component units which have not budgeted for additional uniform contributions. Excludes $58 million annually of estimated AUCs required by municipalities which, if not funded, would further deplete assets in the retirement system.
8. Represents revised estimates of “non-budgeted funds." Excludes any losses from agencies with independent treasuries, which were included in the Krueger Report, based on further diligence and the inclusion of such outflows in other lines (namely, capex).
9. Component unit estimates exclude estimated capital expenditures (which are included in the capital expenditure line) and other delineated expenses and risks, such as the loss of ACA funding. Once these items are accounted for, the total impact of the component units on the overall financing gap is negative.
10. Capital expenditures based on GDB forecast of recommended projects not available at the time of the Krueger Report and includes maintenance capex and capex related to regulatory compliance, construction in progress, judgements, emergencies, and extraordinary maintenance and repairs. Does not include municipal capital expenditures, which have historically been largely funded by the Commonwealth via bond issuances and GDB credit facilities.
11. Unadjusted since the Krueger Report.
12. HTA expenditure includes highway and Tren Urbano disbursements, excluding capital expenditures and debt service and including the payment of past-due payables. Tren Urbano related disbursements after FY16 represent pay-down of past due payables, but not ongoing operating costs.
13. Per revised estimates based on further diligence done on ASES.
14. The currently estimated range of the impact of the loss of Act 154 is $650 million to $1,500 million. For illustrative purposes, the midpoint of this potential loss is included in the projections (with a half year impact assumed for 2018).
15. Included debt service payments related to GO, GDB, PBA, PFC, COFINA, PRIFA, UPR, PRCCDA, PRIDCO, GSA, PRIFA BANs, ERS, and HTA. PRIFA BANs are on accelerated schedule with excess cash flow sweeps as estimated by GDB. Note that the Krueger Report had netted the PRIFA BANs from the GDB net operating revenues and had embedded ERS debt service in the retirement shortfall estimate.
16. Accounts payable includes amounts owed to General Fund third parties, tax refunds, PRASA, PREPA, and police officer litigation. Excludes pay-downs by component units and HTA, which are embedded in the forecasts for those entities.
17. Amount required for GDB to meet its estimated minimum statutory liquidity requirement of $350 million and the Commonwealth to have $1.0 billion of total deposits on hand by the end of FY 2016 and $1.5 billion by the end of FY 2017.
18. Identified inflows from entities outside the model (primarily SIF) that are used to cover certain General Fund related expenses in FY 2016. These expenses are included in the "General Fund Budget" line.
19. Ratio based on total revenues shown less Federal Transfers. Note that in the build to total revenues GDB net operating revenue includes certain deposit outflows. Additionally, PRIDCO revenues are embedded in the net operating deficit of component units, not in revenues, though its debt service is included in the consolidated interest and principal line items. Also note that any UPR revenues are not included as they are assumed to be offset with other UPR expenses consistent with the Krueger Report approach (appropriations to UPR are included as outflows in the model).