March 10, 2017

Re: February 28, 2017 Fiscal Plan
for the Commonwealth of Puerto Rico

To the Members of the Oversight Board:

OppenheimerFunds, Franklin Advisers, and the First Puerto Rico Family of Funds are retail municipal bond investors with over $10 billion invested in Puerto Rico and its public corporations. For decades, we have provided financing for much of Puerto Rico's critical capital needs, and we view our interests to be closely aligned with those of the people in Puerto Rico.

We write regarding Puerto Rico's Fiscal Plan, dated February 28, 2017. We appreciate the work that the Rosselló Administration has put into the Fiscal Plan in the short time since it took office. We believe this Fiscal Plan represents a real improvement over the prior administration's drafts, particularly in its Fiscal Plan's focus on implementing operational reforms and commitment to reducing subsidies.

We agree with the Oversight Board that there is still work to be done on the Fiscal Plan. As the Oversight Board points out, there are areas of the Fiscal Plan that require additional "specificity, scale and timing."[1] Puerto Rico admits that its designation of services as essential or non-essential is still "under development,"[2] and that it is still deciding how to replace the Act 154 excise tax.[3] One of the biggest variables in the Fiscal Plan – the level of healthcare funding that Puerto Rico receives, which will have a "substantial financial impact"[4] – is unresolved. Without clear answers on healthcare funding, it is impossible to get a real picture of Puerto Rico's revenues and expenses.

Even if these issues were all resolved, the Commonwealth and the Oversight Board have clear areas of disagreement on Puerto Rico's economic projections and the underlying numbers. We believe that the significant open issues and areas of disagreement between the Oversight Board and the Commonwealth on assumptions and other key aspects of the Fiscal Plan call for an extension of deadlines regarding the Fiscal Plan.

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[1] Letter from Hon. José B. Carrión III, Chair, Fin. Oversight & Mgmt. Bd. for Puerto Rico, to Hon. Ricardo A. Rosselló Nevares, Governor, P.R. 3 (Mar. 9, 2017), https://junta.pr.gov/wp-content/uploads/wpfd/50/58c1e7d75ab33.pdf.

[2] Fiscal Plan, Puerto Rico Fiscal Agency and Financial Advisory Authority 120 (Feb. 28, 2017), https://junta.pr.gov/wp-content/uploads/wpfd/50/58b79bb6009fd.pdf.

[3] Fiscal Plan at 26.

[4] Fiscal Plan at 89.

An extension would also allow Puerto Rico and the Oversight Board to work with Puerto Rico's key stakeholders to develop a Fiscal Plan that makes sense to all the parties.

Giving creditors access to information and making sure the parties agree on that information and the assumptions behind it is usually the first step in any reorganization. We already have serious questions about the numbers and assumptions in the Fiscal Plan and in the Oversight Board's letter and no independent visibility into how those numbers and assumptions are reached.[5] Even experts with access to all information – the Oversight Board's expert, Ernst & Young, and the Commonwealth's expert, Conway Mackenzie – disagree. The first step here needs to be for the Oversight Board, the Commonwealth, and creditors to work together to reach an agreement on these important financial issues. Only once these issues are resolved can the parties engage in good faith negotiations.

We recognize that this requires additional time. We strongly urge the Oversight Board to postpone the March 11 fiscal plan re-submission deadline and the March 15 Fiscal Plan certification deadline. We also support an extension of the PROMESA stay until December 31, 2017, as requested by Governor Rosselló, to allow Puerto Rico to reach a resolution on many of the open issues and put together a complete Fiscal Plan that resolves the uncertainties in this draft.[6]

We take this opportunity to point out some of these areas of the Fiscal Plan that we believe need work and would benefit from creditor input.

We believe this Fiscal Plan will not provide Puerto Rico with access to the capital markets. The Fiscal Plan does not respect existing law and priorities and commitments established under those laws. For instance, it includes money validly transferred to COFINA as part of the Commonwealth's baseline revenues. Regaining "adequate access to short-term and long-term credit markets at reasonable interest rates"[7] requires restoring investor confidence in the rule of law and demonstrating a commitment to valid pledges of collateral, not destroying valid, long-standing structures like COFINA.

The Fiscal Plan does not ensure that assets of a territorial instrumentality are not used for the benefit of the covered territory, nor does it respect lawful liens and priorities.[8] Contrary to the Oversight Board's assertion,[9] there is sufficient data to determine the

[5] We attach a preliminary, high-level diligence list that our advisors have put together, and which we are sending to the Commonwealth's advisors, as an example of the types of information that are necessary for creditors to understand the Fiscal Plan.

[6] This is our view as holders of Puerto Rico debt other than PREPA debt. We believe that PREPA does not require this extra time and that the PREPA deal should move forward.

[7] Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), Pub. L. No. 114-187, § 209(*1*), 130 Stat. 549 *et seq.* (2016) (to be codified at 48 U.S.C. § 2101 *et seq.*).

[8] *See* PROMESA §§ 201(b)(1)(m), (n).

Fiscal Plan's noncompliance. The Fiscal Plan does not distinguish between general fund revenues and revenues that are pledged to bondholders. It aggregates the full sales and use tax into its revenue projections, in the face of the transfer of a portion of the sales and use tax revenues to COFINA and liens granted to COFINA bondholders by the Commonwealth, endorsed by senior officers of multiple administrations from both sides of the aisle, and in place for ten years. It makes all expenses senior to debt service on general obligation bonds, despite constitutional and statutory protections. It also aggregates other revenue streams pledged to bondholders – i.e., "clawback" revenues like toll revenues, rum taxes, or hotel occupancy taxes – into regular revenue projections in the face of existing laws and agreements that restrict its use to payment of debt service on certain bonds or, if other sources of revenue are depleted, the general obligation bonds.

The Fiscal Plan does not include a real debt sustainability analysis.[10] The debt sustainability analysis in the Fiscal Plan is simply a calculation of estimated revenues left over for debt service after the payment of all government services. It does not reflect any substantive analysis or proposal on adjustment of debt.

PROMESA requires that a fiscal plan ensures that Puerto Rico will "achieve fiscal responsibility" while paying the government's "essential services."[11] Taken together, these sections require that Puerto Rico pay as much as it can to bondholders, not as little as it can.[12] But the Fiscal Plan instead provides for the funding of all services, with left over money to go to debt service – effectively subordinating these expenditures to all other government expenditures and making them contingent on healthcare subsidies.

The Fiscal Plan ignores important revenue and expense measures that should be taken. Revenues before revenue-enhancement measures are expected to decline in certain years – despite recent collections data and without substantiation by any econometric analysis – and show essentially no growth in consolidated revenues over a 10-year forecast horizon. We disagree with this assumption. Even in the absence of agreement on economic growth projections and the real amount of expenses, the Fiscal Plan is missing important detail on measures that are supposed to help economic growth. The Commonwealth also has additional steps it should take to increase revenue and reduce expenses, such as adopting some of the key

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[9] Oversight Board Letter at 1 n.1.

[10] *See* PROMESA §§ 201(b)(1)(E), (I).

[11] PROMESA §§ 201(b)(1)(A), (B).

[12] This is also true in the context of a Title III proceeding. Chapter 9 of the Bankruptcy Code requires that a plan be in the "best interests" of creditors. 11 U.S.C. § 934(b)(7). According to legislative history, this test requires a municipality to make a detailed showing that it has done what it can to pay creditors. 124 CONG. REC. H11,100 (Sept. 28, 1978); S17,417 (Oct. 6, 1978). PROMESA makes this requirement explicit, by requiring a court to consider whether "available remedies under the non-bankruptcy laws and constitution of the territory would result in a greater recovery for the creditors than is provided in" a proposed Title III plan. PROMESA § 314(b)(6).

tax reform initiatives that the Commonwealth's own consultants recommended, which would dramatically boost overall collections.[13]

This letter provides only a few of our concerns with the Fiscal Plan. We urge the Oversight Board to give Puerto Rico more time to present a Fiscal Plan that includes resolution of the open issues between the Oversight Board and the Commonwealth and a chance for creditor input.

[13] *See, e.g.*, KPMG, *Unified Tax Code of Puerto Rico: Tax Policy Implementation Options; General Explanation of Principal Options*, COMMONWEALTH OF PUERTO RICO TAX REFORM ASSESSMENT PROJECT (Oct. 31, 2014), http://www.hacienda.pr.gov/sites/default/files/unified_tax_code_of_pr-_general_explanation.pdf.

Sincerely,

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