



GOVERNOR OF PUERTO RICO
Pedro R. Pierluisi

September 12, 2022

VIA ELECTRONIC MAIL

Mr. David A. Skeel, Jr.
Chairman
The Financial Oversight and
Management Board for Puerto
Rico
P.O. Box 192018
San Juan, PR 00919-2018

Re: *Request for Amendments to the Certified Fiscal Plans and Budgets for the Government of Puerto Rico and CRIM*

Dear Chairman Skeel:

As you know, in recent years Puerto Rico's municipalities have faced significant financial challenges due to the budgetary adjustments required under the certified fiscal plans and budgets for the Government of Puerto Rico and the Municipal Revenue Collection Center ("CRIM"). Municipal leaders continue to stress the need for additional funding to carry out their essential government functions that improve the lives of Puerto Rico's residents.

I am aware of the ongoing dialogue between the Financial Oversight and Management Board for Puerto Rico (the "Oversight Board" or the "Board") and the Puerto Rico Mayors Federation and Puerto Rico Mayors Association (collectively, the "Mayors") to develop solutions for the municipalities in financial distress. Our understanding is that those discussions have generally been progressing positively.

In hopes of facilitating important and necessary measures and reforms to strengthen Puerto Rico's municipal structure and funding, I request on behalf of the Government of Puerto Rico, pursuant to PROMESA section 201, that the Board amend (i) the Fiscal Plan for Puerto Rico, as certified on January 27, 2022 ("Commonwealth Fiscal Plan"), (ii) the Commonwealth's Fiscal Year 2023 Budget,



GOVERNOR OF PUERTO RICO
Pedro R. Pierluisi

as certified on June 30, 2022 (the "Commonwealth Budget"), (iii) the Fiscal Plan for CRIM, as certified on May 20, 2022 (the "CRIM Fiscal Plan"), and (iv) CRIM's Fiscal Year 2023 Budget, as certified on June 30, 2022 (the "CRIM Budget," and collectively, the "Commonwealth and CRIM Fiscal Plans and Budgets"), to implement a three-pronged approach that I believe will promote the flourishing of Puerto Rico's municipalities. As discussed in more detail below, the Government's proposal seeks to (a) allow AAFAF to advise, assist and provide technical assistance to municipalities in the development and implementation of measures and reforms to achieve efficiencies and fiscal sustainability, (b) authorize Intergovernmental Transfers to create a new Municipal Essential Services Fund to ensure the funding of essential public services at the local level, and (c) eliminate the municipalities' payments to ASES, which should be funded by the Government.

I. Allow AAFAF to Advise, Assist and provide Technical Assistance to Municipalities

Since the commencement of Puerto Rico's Title III cases, the Oversight Board has expressed concerns regarding the long-term strengthening of Puerto Rico's 78 municipalities and the development of administrative efficiencies to improve fiscal responsibility at the local level, without jeopardizing the provision of essential services at the municipal level. In prior fiscal year budgets, the Board provided for additional funding to municipalities through the Municipal Service Consolidation Fund upon the achievement of certain milestones designed to promote the consolidation and optimized administration of the municipalities. However, access to the Municipal Service Consolidation Fund has been limited by the implementation of complex guidelines.

To facilitate the consolidation and implementation of administrative efficiencies at the municipal level, the Government proposes that the Board allow AAFAF to assist the municipalities with the process of improving and consolidating their administrative functions. In that role AAFAF would work with the municipalities to propose amendments to the Board's existing Municipal Service Consolidation Fund guidelines and discuss and develop implementation plans with the municipalities. We believe that AAFAF's centralized leadership and expertise in creating fiscal solutions will help accelerate the administrative and back-office consolidations that the Board has sought over the last five years. To further these efforts, the Government requests the Board to provide AAFAF with access to the \$66 million of prior funding for the Municipal Service Consolidation Fund, which



GOVERNOR OF PUERTO RICO
Pedro R. Pierluisi

would allow AAFAF to accomplish these administrative efficiency goals quickly and effectively, subject to the approval of new guidelines.

II. Authorize Intergovernmental Transfers to create the new Municipal Essential Services Fund.

Puerto Rico's municipalities have historically relied on the Government's financial allocations to ensure the delivery of accessible and affordable public services, including, and not limited to, policing, sanitation services, garbage collection, and emergency services. These are all essential public services required to be provided for under fiscal plans and budgets pursuant to PROMESA sections 201(b)(1)(B) and 201(c)(1).¹ During the Government's fiscal crisis, liquidity constraints and an economic recession led the Government to reduce intergovernmental transfers to municipalities.

As you know, on January 18, 2022, the Title III Court confirmed the *Modified Eighth Amended Title III Joint Plan of Adjustment of the Commonwealth of Puerto Rico, et al.* (the "Commonwealth Plan of Adjustment"), which became effective on March 15, 2022. As a result of the plan's effectiveness, Puerto Rico is no longer facing the unsustainable debt burden that caused it to seek Title III relief in 2017. Similarly, improvement in Puerto Rico's economy has resulted in revenue collection outperformance, thus creating primary surpluses and providing unprecedented liquidity to the Government. As can be seen in the Treasury Single Account ("TSA") FY2022 Cash Flow as of June 24, 2022, the year-to-date outperformance in the TSA relative to the revised liquidity plan was \$3.2 billion. While some of this outperformance may be timing related and some needs to be distributed on account of the Commonwealth's New CVI Bonds and AFSCME bonuses, a considerable amount remains available.

Despite these seismic changes to Puerto Rico's economic circumstances, the Commonwealth Fiscal Plan continues to deprive Puerto Rico's municipalities of adequate financial support to allow them to reestablish or normalize the essential services they provide to their residents. The reduced appropriations to the

¹ 48 U.S.C. § 2141(b)(1)(B) ("A Fiscal Plan developed under this section shall . . . ensure the funding of essential public services . . ."); 48 U.S.C. § 2142(c)(1) ("the Oversight Board shall determine in its sole discretion whether each proposed Budget is compliant with the applicable Fiscal Plan . . .").



GOVERNOR OF PUERTO RICO
Pedro R. Pierluisi

municipalities have exacerbated their financial distress, which continues to negatively impact their day-to-day functions and the delivery of essential services to Puerto Rico residents. The Government believes that reasonable and fiscally responsible changes to the Commonwealth and CRIM Fiscal Plans and Budgets can remedy this situation.

My administration proposes the creation of a Municipal Essential Services Fund, to be funded from the Government's net annual surplus (after all payments mandated Commonwealth Plan of Adjustment) at an amount of approximately 25% of such surplus, with a cap of \$150 million per year. This modest increase in municipal intergovernmental transfers is fair, reasonable and conservative, especially when considering the additional expenses that the municipalities have assumed over the past decade, including the assumption of the PayGo and healthcare costs. In fact, it would only represent approximately 1% of the Government's current own-source revenues.

Since the Board started exercising its powers pursuant to Sections 201 and 202 of PROMESA, the Board has reduced municipal appropriations by approximately 73%, from \$330 million in FY2017 to only \$88 million in FY2022. This reduction is unprecedented when compared to the level of funding that U.S. states provide to their local governments. For example, the average share of own-source revenue sent to local governments among all U.S. mainland states is approximately 48%.² If the proposed surplus amounts are contributed to this new Municipal Essential Services Fund, the Government would still only be allocating approximately 1% of its own-source revenue to municipal support, which is a mere fraction when compared to the U.S. average. The Government does not request funding to comparable levels to U.S. local governments as it is cognizant that mainland localities shoulder larger responsibilities to service their local residents, as compared to Puerto Rico's municipalities. Nevertheless, I believe that the request for a 1% level of funding, subject to the availability of a surplus, is clearly reasonable.

The impact of this modest investment in our municipalities cannot be overstated: it will ensure that all municipalities can continue to provide essential services

² See National Conference of State Legislatures (NCSL) report titled "State Aid to Local Governments."



GOVERNOR OF PUERTO RICO
Pedro R. Pierluisi

without the need to institute additional cuts or potentially seek future relief under Title III of PROMESA, a cost that ultimately will be borne by the Government. Additionally, there is the risk of losing hundreds of millions of dollars in federal funds if municipalities collapse or are forced to downsize to a level where they are unable to comply with federal requirements. The Government believes that given the different economic and fiscal realities of Puerto Rico, increased municipal appropriations are a goal that both the Government and the Board should share and work to achieve. A reasonable compromise on this issue is achievable and is in the best interests of the people of Puerto Rico.

III. The Municipality Payment to ASES for Municipal Medical Insurance Should Be Funded by the Government.

Currently, CRIM is responsible for remitting payments on behalf of the municipalities to fund the Puerto Rico Health Insurance Administration ("ASES") in accordance with the Commonwealth Fiscal Plan and CRIM Fiscal Plan. Those fiscal plans include temporary relief for municipal ASES contributions to reflect any additional funds made available by the federal government using a Federal Municipal Adjustment Percentage ("FMAP") calculation. For FY2023, the Commonwealth and CRIM Fiscal Plans estimate the municipalities' ASES obligation to be approximately \$164 million, before applying any adjustments based on an FMAP above 55%. Although the fiscal plans also allow for additional offsets based on any incremental federal funds that become available during FY2023, the municipalities' ASES contributions continue to be a drain on their limited resources.

The Government requests that the Commonwealth and CRIM Fiscal Plans and Budgets be amended so that Government funds the ASES contribution on behalf of all municipalities. The municipalities' ASES contribution, at the onset, was based on the Government's need for additional funds to provide Medicaid services to its citizens. Given this background and Puerto Rico's continued receipt of federal funds for Medicaid at elevated levels, as a matter of fairness, the municipalities should no longer contribute to this program. The incremental cost associated with this amendment is estimated to be, at most, approximately \$164 million per year or \$820 million over the next 5 years from FY2023-FY2027.



GOVERNOR OF PUERTO RICO
Pedro R. Pierluisi

My administration believes that fiscal support for our municipalities is long overdue and our proposed modest changes to the Commonwealth and CRIM Fiscal Plans and Budgets would ensure that the essential services provided by our municipalities can continue without interruption. I request that the Board schedules a meeting with Secretary of State Omar Marrero and the Mayors' representatives to discuss these proposals, in order to achieve reasonable and fiscally responsible solutions for Puerto Rico's municipalities. Once the Board confirms its availability, this working group will share their findings, data and presentation.

As always, I look forward to continuing to collaborate with you to achieve our common goals for the benefit of the people of Puerto Rico.

Sincerely,

A handwritten signature in blue ink, appearing to read "Pierluisi".

cc: Hon. Omar J. Marrero
Andrew G. Biggs
Arthur J. González
Antonio L. Medina
John E. Nixon
Justin M. Peterson
Betty A. Rosa
Jaime El Koury, Esq.
Hon. Gabriel Hernández, Federation of Mayors
Hon. Luis Javier Hernández, Association of Mayors
Julian Bayne, Esq.