

**FINANCIAL OVERSIGHT AND MANAGEMENT BOARD  
FOR PUERTO RICO**



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*Natalie A. Jaresko*  
Executive Director

BY ELECTRONIC MAIL

February 5, 2018

The Honorable Ricardo A. Rosselló Nevares  
Governor of Puerto Rico  
La Fortaleza  
P.O. Box 9020082  
San Juan, PR 00902-0082

Dear Governor Rosselló Nevares:

The Board is in receipt of PRASA's proposed fiscal plan, dated January 24, 2018 (the "Proposed Plan"), and recognizes the substantial revisions that PRASA has made to the existing revised fiscal plan, certified by the Board on August 25, 2017 (the "Current Plan"), to adjust for the post-Hurricane Maria reality. Nonetheless, the Board has determined that the Proposed Plan requires certain revisions before the Board can certify it as compliant with the requirements of the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"). This letter will serve as the notice of violation provided for in Section 201(c)(3)(B)(i) of PROMESA. The Board looks forward to continuing to discuss the Proposed Plan, and the violations detailed herein, with you in the coming weeks.

Specifically, the Proposed Plan forecasts significantly reduced revenues post-Hurricane Maria but does not provide for a commensurate reduction in operating expenses, which results in a significant operating deficit. Similarly, PRASA presently faces a precarious liquidity shortfall and must adopt a cash management program to actively minimize the cash gap. It is more clear than ever that water quality is key to quality of life for residents and cost of doing business for the economy. The Proposed Plan demonstrates that PRASA is committed to achieving a more resilient water system and improved water quality but it must provide more detail on the water quality initiatives and infrastructure investment plans.

PROMESA provides the Government with a powerful tool to restore economic growth and opportunity to the people of Puerto Rico. The Board urges the Government to use this tool to provide for a sustainable fiscal future for PRASA and to further the goal of providing more affordable water services, improved water quality, and a more resilient water infrastructure.

### ***Baseline***

The Board requires four changes to baseline projections:

- **Cash management<sup>1</sup>:** While PRASA has been able to delay the day on which it reaches a negative cash balance, it still requires aggressive cash management to maintain liquidity. PRASA must add a chapter to the Proposed Plan detailing its cash management program through December 2018. The program should show all anticipated cash flows and include an aggressive government collections program (e.g., collection of \$25M in past-due central government bills, initiatives to increase government collections rate by 5-10% over current projections), an operating cost reduction program (e.g., for contracted workers or materials and supplies), and an accurate projection of incoming and outgoing funds.
- **Capital improvement plan (CIP)<sup>2</sup>:** PRASA's CIP requires further re-evaluation to maximize use of federal funding and ensure consistency with PRASA's long-term goals. PRASA must revise the Proposed Plan to show a detailed breakdown of and revision to the CIP, eliminating or reducing costs for pre-existing CIP that are superseded or made obsolete by emergency repair projects (e.g., money budgeted for repair and replacement that may no longer be needed), as well as targeting and relating the CIP to enable PRASA to improve water quality and infrastructure resiliency.
- **Future funding<sup>3</sup>:** PRASA must exclude uncertain federal funding sources from the Proposed Plan, including removing the Community Disaster Loan (\$200M) and 50% of the state revolving funds and rural development funds requests (total \$322M).
- **Damage assessment<sup>4</sup>:** Prior to resubmission of the Proposed Plan, PRASA should accelerate damage assessment to provide sufficient time to strategize funding sources and obtain maximum capital funds for stressed infrastructure and provide clarity on reimbursement for repair projects. The Proposed Plan should also thoroughly describe these acceleration efforts and the resulting increase in certainty and clarity to the CIP.

### ***Measures***

The Board requires four changes to revenue and expense measures:

- **Operating expenses<sup>5</sup>:** The Proposed Plan projects that PRASA's baseline revenue will decrease by 17%, driven by hurricane losses, macroeconomic drivers, and lower collection rates. PRASA's Proposed Plan must introduce additional measures to further reduce operational costs given the projected reduced revenues over the next five years to shrink the operating deficit. Where PRASA is limited in its ability to reduce operating

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<sup>1</sup> Section 201(b)(1)(F), (G)

<sup>2</sup> Section 201(b)(1)(J)

<sup>3</sup> Section 201(b)(1)(A), (G)

<sup>4</sup> Section 201(b)(1)(J), (L)

<sup>5</sup> Section 201(b)(1)(D), (G)

expenditures, it should thoroughly explain those limitations and identify alternative expenditure reduction.

- **Long-term vision<sup>6</sup>:** PRASA must provide a vision for and perspective on potential actions it may take to achieve long-term fiscal sustainability, improved water quality, and greater infrastructure resiliency. The Proposed Plan must include a chapter describing this long-term vision and a prioritized capital plan to achieve it with specific measures around, for example, infrastructure consolidation, modernization, interconnection, and digitalization. The Proposed Plan should propose potential funding sources for the capital plan, including but not limited to federal funding, additional P3s, and concessions.

### *Other*

The Board requires the following other change to the Proposed Plan:

- **Debt sustainability analysis<sup>7</sup>:** The Proposed Plan must include a more specific analysis of PRASA's 30-year debt sustainability projections, including specific assumptions related to macroeconomic projections and the projected costs of pension liabilities. Rather than include a range of potential debt service, the plan should outline specific debt capacity year-on-year.
- **Time horizon<sup>8</sup>:** Upon further reflection, the Board has determined that the Proposed Plan must extend through FY23.
- **Included entities<sup>9</sup>:** The Proposed Plan must include each component unit and subsidiary of PRASA.

### *Conclusion*

The Board recognizes the difficulties implicit in these policy decisions, as well as the long path to return PRASA to fiscal stability. Reaching this goal will take time, enormous effort and the full commitment of PRASA's and the Government's leadership, but done properly and in a sustained manner it will put PRASA on the path to a better future. The Board specifies 6:00pm AST on February 12, 2018 as the deadline for submitting a revised, proposed fiscal plan, including all financial models.

Sincerely,



José B. Carrión III  
Chair

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<sup>6</sup> Section 201(b)(1)(D), (G), (J)

<sup>7</sup> Section 201(b)(1)(I)

<sup>8</sup> Section 201(b)(2)

<sup>9</sup> Section 201(b)(1)(A), (F), (L)

Hon. Ricardo A. Rosselló Nevares

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