



Financial Oversight & Management Board for Puerto Rico


Annual Report

Fiscal Year 2018

July 30, 2018

In accordance with Section 208(a) of the Puerto Rico Oversight, Management, and Economic Stability Act (“PROMESA”), I am pleased to present the second Annual Report of the Financial Oversight and Management Board for Puerto Rico (the “Oversight Board”). As required by Section 208, this Annual Report is being provided to the President, Congress, the Governor, and the Legislature.

Sincerely,

A handwritten signature in black ink, appearing to read 'J. Carrión III', with a long horizontal flourish extending to the right.

José B. Carrión III
Chair

Andrew G. Biggs
Carlos M. García
Arthur J. González
José R. González
Ana J. Matosantos
David A. Skeel, Jr.

CC: Natalie A. Jaresko
Christian Sobrino Vega

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Executive Summary

The Oversight Board continued to make progress in its second year toward fulfilling its statutory mandates of helping Puerto Rico to achieve fiscal responsibility, regain access to capital markets, restructure its outstanding debt, and return to economic growth. While the catastrophic devastation caused by Hurricanes Irma and Maria utterly upended the daily lives of all Puerto Ricans and the work of the Oversight Board, the Oversight Board also rose to the challenge by assisting the Government of Puerto Rico in its disaster response and recovery efforts while tackling its fiscal oversight, financial management, and debt restructuring, responsibilities.

Immediately after Hurricanes Irma and Maria struck, the Oversight Board provided the Government with the flexibility to reappropriation up to \$1 billion in budgeted expenditures to cover disaster related expenses. The Oversight Board also worked with the Government to forecast the liquidity needs of the Government in the months ahead, which eventually led to Congress providing Puerto Rico with access to specialized forms of Community Disaster Loans to offset the projected revenue shortfalls caused by the hurricanes.

Because Hurricanes Irma and Maria defined a new reality for Puerto Rico, the Oversight Board also initiated the process of rewriting the fiscal plans for the Commonwealth and the covered instrumentalities. What followed was a several-month long interactive and collaborative engagement between the Oversight Board, Government, and various stakeholders including academics, the public, private industry, and creditors, which eventually led to the Oversight Board certifying fiscal plans that it developed. The overarching goals of the fiscal plans are to fulfill PROMESA's mandates, which requires a series of ambitious structural reforms and fiscal measures to restore growth and opportunity to the people and businesses of Puerto Rico. With the fiscal plans certified, the Oversight Board proceeded to developing budgets for the Commonwealth and the various instrumentalities. The budgets that the Oversight Board certified are consistent with the fiscal plans and contain numerous budgetary controls to improve fiscal management, monitoring, and transparency. Because the fiscal plans and budgets were certified at the very end of the fiscal year, the most critical phase – implementation – has just begun. The Oversight Board will be monitoring and assisting as the Government implements fully the fiscal plans' measures and reforms.

Certifying revised fiscal plans also allowed the Oversight Board to reengage with creditors in earnest to achieve consensual restructurings of Puerto Rico's debt. The Government is in the process of securing a final resolution to the Title VI restructuring of the Government Development Bank's debt and the Oversight Board made significant progress with creditors for COFINA, the Sales Tax Financing Corp., and PREPA, the Puerto Rico Electric and Power Authority. With the help of federal mediators, the Oversight Board and Government continue to negotiate with Puerto Rico's creditors to reach sustainable resolutions to Puerto Rico's staggering debt burden.

Introduction

The Oversight Board is pleased to submit its second Annual Report. As required by Section 208(a) of PROMESA, the report covers:

- (1) the progress made by the Government of Puerto Rico in meeting the objectives of PROMESA;
- (2) the assistance provided by the Oversight Board to the Government of Puerto Rico in meeting the purposes of PROMESA;
- (3) recommendations to the President and Congress on changes to PROMESA, other Federal laws, and Federal actions that would assist the Government of Puerto Rico in complying with the Fiscal Plan;
- (4) the manner in which the Oversight Board has spent funds allocated to it; and
- (5) other activities of the Oversight Board.

PROMESA was signed into law by President Barack Obama on June 30, 2016 and he appointed the seven members of the Oversight Board on August 31, 2016. At that time, Puerto Rico had accumulated over \$50 billion in unfunded pension liabilities and over \$70 billion of debt, and was facing an imminent default. The Oversight Board was created to restructure Puerto Rico's staggering debt burden and restore sustained economic growth to Puerto Rico so that the Government of Puerto Rico could achieve fiscal balance and access to the capital markets.

As discussed in last year's Annual Report, the Oversight Board worked with the Government of Puerto Rico to create and certify the first fiscal plans for the Commonwealth and its instrumentalities. The Oversight Board also filed for Title III for the Commonwealth, COFINA, PREPA, the Highway and Transportation Authority, and the Employee Retirement System.

In September 2017, shortly after the Oversight Board submitted its first Annual Report, Hurricanes Irma and Maria struck the Island, causing unprecedented humanitarian, economic, and infrastructure-related damages and upending the daily lives of Puerto Rico's over 3 million residents. Thousands of residents were left homeless, basic utilities were completely shut down (and took months to become operational), and schools, hospitals, and businesses were destroyed. Tens of thousands of Puerto Ricans fled the Island. The Federal Government's response has become one of the largest and most complex disaster recovery efforts in U.S. history.

The Oversight Board's second year was in many respects defined by the new reality that Hurricanes Irma and Maria created for Puerto Rico. During this past fiscal year, the Oversight Board also redoubled its work toward improving fiscal governance, accountability, and internal controls; made progress toward restructuring Puerto Rico's debt fairly and sustainably; and initiated an investigation into Puerto Rico's past debt issuance practices.

Progress by the Government of Puerto Rico

This past fiscal year has been a momentous one for the Government and people of Puerto Rico. It was the first full fiscal year of this Administration and the year in which the most powerful hurricane to strike the Island in a hundred years caused unprecedented, catastrophic damage. Accordingly, the Government's progress toward meeting the objectives of PROMESA came in fits and starts, in many instances due to factors outside of its control, but sometimes due to the Government's own choices. Below is a timeline of major events to give a sense of that progress.

- July 2017: After the Oversight Board certified the budget for FY2018, the Government began implementation. Pursuant to the fiscal plan for the Commonwealth that the Oversight Board certified, the Government was required to submit sufficiently detailed liquidity and implementation plans to demonstrate that it would produce the levels of increased revenues and savings in Government that the budget and fiscal plan required.
- August 2017: The Oversight Board determined that the Government had failed to provide the requisite liquidity and implementation plans to achieve the savings in Government spend that the budget and fiscal plan required. This triggered a requirement that the Government institute furloughs to generate the requisite savings. After the Governor refused to initiate furloughs, the Oversight Board filed a lawsuit to compel him.
- September 2017: Hurricanes Irma and Maria brought unimaginable humanitarian, economic, and infrastructure-related damage and upended the daily lives of Puerto Rico's over 3 million residents. Thousands of residents were left homeless, basic utilities were completely shut down (and took months to become operational), and schools, hospitals, and businesses were destroyed. Tens of thousands of Puerto Ricans fled the Island. Amidst this chaos and suffering, the Oversight Board withdrew its furloughs-related lawsuit.
- October 2017: As the Government worked to provide emergency and basic services to its citizens, the Oversight Board began the formal process of revising the fiscal plans for the Commonwealth and the various instrumentalities.
- November 2017: Working with the Oversight Board, the Government projected its potential liquidity needs due to the anticipated increased expenditures and decreased revenues associated with Hurricanes Irma and Maria. This work eventually led to Congress creating a new Community Disaster Loan program for Puerto Rico to provide that emergency liquidity relief.
- December 2017: Working with the Oversight Board, the Government publicly announced that it became aware of hundreds of previously undisclosed bank accounts and that it was in the process of locating and assessing the source and character of each. The Oversight Board announced that it was launching a forensic analysis of the bank accounts.
- January 2018: The Governor announced that he would transform PREPA by entering into a long-term concession with a private company for the transmission and distribution, and

a privatization of the generation. The Oversight Board immediately supported the Governor in these efforts.

- February-March 2018: As part of a highly collaborative and interactive process with the Oversight Board, the Government developed and submitted multiple drafts of fiscal plans for the Commonwealth and its instrumentalities. These fiscal plan drafts contained several structural reforms such as energy sector transformation, labor and welfare reform, and ease of doing business reform, as well as fiscal measures to rightsize the Government.
- April 2018: The Oversight Board certified the fiscal plans for the Commonwealth and its instrumentalities. Most of the measures and reforms contained in each of the fiscal plans were identical to what the Government submitted. Nonetheless, the Oversight Board certified fiscal plans that it developed because the Oversight Board determined, in its sole discretion, that additional or different measures and reforms were needed to satisfy PROMESA.
- May 2018: The Governor and the Oversight Board came to an accommodation that would result in the Oversight Board revising the Commonwealth fiscal plan to incorporate certain measures that the Governor requested while the Governor would push for the repeal of a territorial law that stood in the way of the most significant structural reform – labor reform – being realized. The Governor submitted a proposed budget for the Commonwealth and the instrumentalities.
- June 2018: The Legislature passed and the Governor signed into law the legislation that authorizes and provides the framework for the PREPA transformation transaction. The Legislature passed and the Governor signed into law the legislation that authorizes and provides the framework for the restructuring of GDB. The Legislature submitted a proposed budget for the Commonwealth. The Oversight Board certified fiscal plans and budgets for the Commonwealth and the instrumentalities.

Assistance Provided by the Oversight Board

I. Certifying Revised Fiscal Plans

As described in the Introduction to this Annual Report, Hurricanes Irma and Maria struck Puerto Rico just months after the Oversight Board had certified fiscal plans for the Commonwealth and its instrumentalities. Given the widespread devastation to personal and public capital and property, disruption of business activity, and outmigration of a significant part of the population, the Oversight Board determined that the fiscal plans had to be updated to reflect the new macroeconomic and fiscal realities of the Island.

At the outset of the fiscal plans revision process, the Oversight Board enumerated several principles that would guide its certification decisions:

- 1) Fiscal Plans should reflect updated macroeconomic and demographic trends of the Island, including projected disaster funding, damage assessments, and implied size of government
- 2) Fiscal Plans should include resources to address and track emergency response, given the likelihood of future natural disasters
- 3) In the development of the Commonwealth Fiscal Plan, structural reforms – key changes needed to create economic growth – should be prioritized given the new and more dire growth trajectory of the Island after the storms
- 4) Capital expenditure plans should focus on long-term recovery and restoration of critical infrastructure, rather than just relying on short term inflows of disaster funding to rebuild
- 5) Plans should achieve structural balance as soon as possible, and no later than FY2023
- 6) Fiscal Plans should include a 30-year debt sustainability analysis to aid in the debt restructuring process

Throughout the nine months following Hurricanes Irma and Maria, the Government and Oversight Board worked hand in hand to develop the Fiscal Plans. The Governor and members of the Oversight Board held numerous formal meetings, staff and advisors for the Government and Oversight Board collaborated in joint working groups that spanned every aspect of the fiscal plans, and the Oversight Board held multiple listening sessions with external stakeholders, the public, and creditors. The Government and Oversight Board eventually reached broad agreement on most aspects of each fiscal plan.

In the case of the Commonwealth Fiscal Plan, the Oversight Board and Governor agreed that labor and welfare reform, ease of doing business reform, energy reform, and infrastructure reform were the crucial structural reforms that had to be adopted in order to create long-lasting, robust economic growth. They also agreed on the need to transform the local healthcare system to control healthcare inflation, generate efficiencies in executive agencies through consolidations and rightsizing of

services, reduce appropriations to municipalities and the University of Puerto Rico so that they could become more self-sustainable and ease the Commonwealth of its burden to subsidize them, and increase revenues through improving taxpayer compliance and instituting new or increased taxes and fees.

However, the Governor also disagreed with a number of reforms in the Commonwealth Fiscal Plan. The Oversight Board has made pension reform a priority because of the glaring underfunding of the public pension systems (more than \$50 billion) that have left the plans without the resources to keep the promises that were made to current and future retirees. To deal with this problem, the Oversight Board has called for (i) freezes on the existing pension systems, (ii) conversions of those pension systems to defined contribution plans, and (iii) an average reduction in benefits of approximately 10%. The reductions would be implemented progressively to protect lower-income retirees from poverty, thereby requiring larger reductions from retirees with the highest benefits. Under the formula outlined by the Oversight Board, 25% of retirees will experience no reductions and the median retiree will receive less than a 10% reduction. While the Government agrees with parts one and two of the pension reform, it has refused to pursue the third part.

While the Government and the Oversight Board agreed on some aspects of labor reform, such as the creation of an Earned Income Tax Credit and addition of a work requirement for NAP, the Government initially rejected the most critical component of labor reform – changing the law of Puerto Rico to make it an at-will jurisdiction for private sector employees like 49 of the 50 states. The Governor and Oversight Board eventually reached an accommodation that resulted in the Oversight Board reducing certain budget cuts in exchange for the Governor’s support to make Puerto Rico an at-will employment jurisdiction. Unfortunately, the Legislature failed to pass the necessary legislation, leaving Puerto Rico’s labor laws as-is, and not taking action to increase Puerto Rico’s exceptionally low labor market participation rate.

At the conclusion of this months-long collaborative process with the Government, the Oversight Board developed and certified its own fiscal plan for the Commonwealth. While this fiscal plan contains many of the fiscal measures necessary to rightsize the Government, it contains only those structural reforms that the Government agreed to implement, such as ease of doing business and energy reform, but not comprehensive labor reform because of the Legislature’s failure to pass the requisite legislation. Accordingly, the Commonwealth’s certified fiscal plan projects merely tepid economic growth past FY2023, after the effect of the federal disaster recovery stimulus wares off, and structural deficits after FY2030.

The fiscal plans for the various instrumentalities were similarly the product of a deeply collaborative effort and represent almost complete agreement between the Oversight Board and Government. For PREPA, the Government and Oversight Board agreed on the need and process to transform the Island’s electric grid (discussed further below), although the Government’s fiscal

plan submission omitted important investment and cost savings measures that the Oversight Board required in the certified fiscal plan. With respect to PRASA, the Oversight Board and Government agreed on nearly every reform except for pension reform, given the Government's general refusal to pursue it, and certain other expense measures. For HTA, the Oversight Board required that it adopt an inflation-linked toll increase policy on existing roads but otherwise largely agreed with the Government's proposed fiscal plan. With respect to the University of Puerto Rico, the Government refused to include the necessary revenue and expenditure measures so that the University of Puerto Rico could achieve fiscal balance over the fiscal plan period. Finally, the Oversight Board certified the fiscal plan for GDB as was submitted by the Government.

As the Oversight Board has stated repeatedly, fiscal plans will be revised to reflect material, new information. For example, the Oversight Board expects to revise each fiscal plan this fall once the Oversight Board and Government have the benefit of full FY2018 actuals and updated disaster spending numbers.

II. Certifying Budgets

Unlike last year, in which the Oversight Board reviewed and certified only the General Fund budget for the Commonwealth, for FY2019 the Oversight Board implemented a consolidated budget review process. In addition to the General Fund, the consolidated budget review process includes Special Revenue Funds, Other Funds, and Federal Funds, as well as public agencies without independent fiscal plans. Moreover, the Oversight Board certified budgets for each public corporation with its own fiscal plan. Having a view of the consolidated budget is a major step forward to ensure transparency, monitoring of funds, and above all, to better understand operational trends of the Government. Furthermore, a consolidated budget allows the Oversight Board to measure the Government's progress toward meeting PROMESA's objectives in full.

To engage in this budget process, the Oversight Board developed timelines, guidelines, and key milestones for each budget and worked collaboratively with the Government to scrutinize the FY2018 budget and create a FY2019 consistent with the applicable fiscal plan. The process was a multi-step one. First, the FY2019 budget was created based on the FY2018 budget, taking into account various reapportionments and changes that had been made during FY2018. These changes included updated projections for various expenditures each agency will be responsible for paying in FY2019 that in the past they too often did not make, such as pension contributions and payments to the utilities PREPA and PRASA. Then the Fiscal Plan details were layered on, including (i) macroeconomic assumptions, (ii) revenue projections, (iii) fiscal reforms and expenditure measures, and (iv) fiscal impact of structural reforms. Throughout, the Oversight Board would adjust the budget to reflect new information that it learned from the interactive process with the Government.

The Oversight Board took all steps possible to improve the transparency in the budgets. For example, for FY2019, the Oversight Board allocated the actual utility and rent payments to each agency, which is a departure from the Government's historic practice of under-budgeting payments due and housing them in one account. By doing this, agencies will be more accountable to pay their bills to other public corporations like PREPA and PRASA. Similarly, the Oversight Board allocated pay-as-you-go pension obligations to each agency. These changes will allow for a more transparent budget process and will help the Government have a better view of which agencies are spending within their means, inclusive of all the agencies' payables.

At the conclusion of this process, the Oversight Board determined that the Governor and Legislature submitted non-compliant budgets for the Commonwealth. Accordingly, the Oversight Board developed and certified its own budget resolutions consistent with the Commonwealth's certified fiscal plan. The Oversight Board also included certain oversight language in the budget resolutions for the Commonwealth to enforce financial discipline, establish controls around actual expenditures, and eliminate deficits. As for the public corporations, the Oversight Board determined that the Government had submitted compliant budgets for PRASA and GDB, and therefore the Oversight Board certified the budgets as submitted. The Oversight Board developed its own revised, compliant budgets for PREPA, HTA, and UPR, and submitted them to the Governor.

III. Improving fiscal governance, accountability, and internal controls

One of the Oversight Board's core responsibilities is to improve the Government's fiscal governance, accountability, and internal controls. This is not only a mandatory aspect of a fiscal plan pursuant to Section 201(b)(1) of PROMESA, but is a consistent thread across PROMESA. This past year, the Oversight Board continued to identify and implement structural and process improvements fulfill this mandate.

Perhaps the most critical component of the Oversight Board's efforts in this area in the past year is the build out of the Office of the Chief Financial Officer for Puerto Rico ("OCFO") and its incorporation into the certified fiscal plan for the Commonwealth. The Government previously established the base for the OCFO through an executive order, and the fiscal plan envisions an expansion of the role to implement financial management best practices from other states. In short, the OCFO will centralize all financial management functions, including (i) treasury and liquidity management, (ii) budget development, monitoring, and performance tracking, (iii) maintenance and integration of financial IT systems, (iv) procurement and human resources, (v) financial reporting including timely issuance of the CAFR, and (vi) general management and validation of funds, debt, and financial transactions. This will empower the OCFO to improve fiscal governance and forecasting, increase transparency, substantiate accountability, heighten internal controls, and improve stakeholder confidence in Puerto Rico's financial management. Most importantly, it will

enable the Government to achieve fiscal responsibility and restore access to the capital markets, two cornerstones of PROMESA.

In addition to the OCFO, the Oversight Board established a series of reporting requirements to provide more transparency into the Government's financial management. For example, the Oversight Board created a treasury single account (TSA) reporting requirement for the central Government and the top agencies and public corporations ("component units") within the Commonwealth Fiscal Plan. The reports provide a snapshot of the central Government's liquidity situation as compared to the projected annual liquidity plan. In compliance with the fiscal plan, this report is now publicly reported by the Government on a weekly and monthly basis. Regrettably, the University of Puerto Rico is not complying with the cash and liquidity reporting requirement.

Right after Hurricanes Irma and Maria, preliminary estimates of the liquidity needs were conducted under the assumption that revenues would take a much harder hit than what they actually have. Initial liquidity estimates contemplated the Government having to cover all spending when in fact much of that spending was provided by FEMA in the first instance. These preliminary estimates were done in line with similar hurricane events, such as Hurricanes Katrina and Sandy.

Moreover, the Oversight Board created a Budget-to-Actuals ("B2A") reporting requirement for the central Government and the top twenty component units, as well as the public corporations such as PREPA and PRASA, which has pushed the Government to add resources and capacity to its budgeting and accounting departments. This in turn has enabled the Government to provide greater visibility to stakeholders into its actual spending patterns and an early warning mechanism to alert the Government and the Oversight Board if actual spending deviates from budgeted amounts. In compliance with the fiscal plan, this B2A report is now publicly reported by the Government on a monthly basis.

Other new reporting requirements include: (i) monthly public reporting of pension obligation balances for the Government and public corporations, (ii) monthly public reporting of public employee payroll, headcount, and attendance data, (iii) quarterly reporting on revenue forecasts, and (iv) the full text of all Government contracts and change orders on the Comptroller's website.

The Oversight Board also instituted a holdback provision in the General Fund budget which provides that recipients of appropriations may receive only 95% of their budgeted appropriation, with the remaining 5% held until the final quarter of the fiscal year so that the Government can determine whether revenue will be sufficient to permit the spending of the final 5% of the appropriations in the fourth quarter. The Oversight Board also added a requirement for the Government to provide the Oversight Board with budget projections of revenues and expenditures for each quarter of the fiscal year, which must be consistent with the certified budget. Together

with the report that the Governor must provide under Section 203, the Government is also to provide a quarterly variance analysis that is consistent with modified accrual accounting. In addition, the Oversight Board eliminated the ability to use prior year appropriations beyond the first 60 days of the next fiscal year, to force the Government to close out the prior fiscal year on a timely basis, instituted a requirement that its approval is necessary for any reprogramming of appropriations and of all contracts over \$10 million, and established additional emergency reserves whose use is subject to Oversight Board approval.

Many of these budgetary controls were implemented as a result of the uncertainty around the amount, location, and nature of the Government's various bank accounts. To help provide more clarity on this issue, in January 2018, the Oversight Board retained an independent forensic analysis team to examine the Government's bank accounts and establish an accurate picture of the sources and uses of public funds and any restrictions on those funds. Since then, the independent forensic analysis team has worked with the Oversight Board and AAFAF to execute on a workplan designed to result in the issuance of a report on the accuracy and reliability of financial information published by AAFAF in its periodic Bank Account Reporting. At this stage, the focus of the investigation will prioritize identifying the character of the accounts that have been publicly disclosed.

Finally, the Oversight Board advocated that the Puerto Rico Institute of Statistics (PRIS) be kept as an independent and standalone agency of the Commonwealth and is pleased to see the Government's reconsideration to merge PRIS into other departments. The Oversight Board will work with PRIS to ensure transparency and the improvement of Puerto Rico's statistical capacities. Moreover, in an effort to promote transparency and safeguard public funds, the Oversight Board did not reduce expenditures to key agencies such as the Comptroller and the Ethics Office. The Oversight Board believes that these initial steps will further enhance Puerto Rico's financial stability now as well as the future.

IV. Creditor Negotiations

As provided in PROMESA, debt restructuring negotiations require fiscal plans that identify and project the available resources for debt service. Due to the catastrophic impact of Hurricanes Irma and Maria, the fiscal plans for the Commonwealth and the various instrumentalities had to be revised, as described above. Unfortunately, this deferred the ability of the Oversight Board to make meaningful progress on debt restructuring until new fiscal plans that reflect Puerto Rico's new reality could be certified.

The Oversight Board is pleased to report that last month's certification of updated certified fiscal plans has jumpstarted negotiations over debt restructuring. The Oversight Board maintains that consensual negotiations are always better than contested resolutions, whether in Title VI or Title

III, and believes that substantial progress has been made across Puerto Rico's credits. This is due in part to the tireless efforts of five federal judges who were appointed by the Title III court to act as mediators for the myriad legal disputes arising out of Puerto Rico's debt.

To date, the Government has led the negotiations for entities that are outside of Title III, such as GDB, PRASA, and UPR. As described below, GDB has reached a resolution with its creditors, while PRASA and UPR are in ongoing discussions and currently have forbearance agreements with their respective creditors. The Oversight Board leads negotiations for entities in Title III, such as the Commonwealth, COFINA, and PREPA. As described below, significant progress has been made with COFINA and PREPA and the Oversight Board continues to work toward resolutions for the other Title III entities.

Due in part to the hardship suffered by municipalities from Hurricanes Irma and Maria, the initial Title VI restructuring support agreement negotiated with the creditors of the GDB was revised and simplified. The Puerto Rico municipality creditors of GDB were allowed broader flexibility to offset their deposits at GDB against the amount of loans they owed GDB and were given some additional relief. The GDB's other creditors, including those holding the nearly \$4.2 billion of GDB Notes outstanding, were offered the consensual Title VI opportunity to receive a more simplified new bond secured primarily by cash flow from GDB's portfolio of municipal loans. The GDB's restructuring is proceeding to a Title VI creditor vote in the summer of 2018.

With respect to Title III, numerous mediation sessions and other negotiations took place with creditors this past fiscal year. In connection with the COFINA Title III, the Commonwealth Agent and COFINA Agent that the FOMB appointed to litigate or settle the so-called "Commonwealth - COFINA Dispute" announced a tentative settlement in principle of that dispute in June 2018. Negotiations over that proposal are ongoing in connection with the FOMB's development of the COFINA Title III Plan of Adjustment.

The Oversight Board is also pleased to announce that today it entered into a Preliminary Restructuring Support Agreement ("RSA") with the Ad Hoc Group of PREPA Bondholders, PREPA, and AAFAF. Pursuant to the Preliminary RSA, bondholders will exchange their outstanding PREPA bond debt for two classes of new securitization bonds. The Tranche A bonds will be worth approximately 67.5 cents on the dollar, while the Tranche B "growth" bonds will be tied to the economic recovery of PREPA and mature after 45 years. Unlike previous proposed resolutions with PREPA creditors, this RSA aligns the future debt payments with the reality of the economic recovery of Puerto Rico by requiring a substantial discount and minimizes the long-term financial risk to PREPA ratepayers by setting a fixed transition charge each year to be borne by consumers. The Oversight Board will be working collaboratively with the Ad Hoc Group of PREPA Bondholders on the implementation of the RSA, including the development of a definitive

Agreement, and will continue the dialogue with the monoline insurers and fuel line lenders with the objective of completing a consensual restructuring of outstanding debt.

V. PREPA Transformation

In the aftermath of Hurricanes Irma and Maria, it was clear to all (if it had not been clear already) that PREPA needed to transform itself. Puerto Rico's future economic growth and vitality depends on affordable and reliable power. Yet for too long, electricity provided by PREPA has been expensive and unreliable. PREPA's problems were made incalculably harder by Hurricanes Irma and Maria, which leveled PREPA's infrastructure, knocked out all electricity across the Island and left thousands without power for several months. It was during this time that the Governor proposed and the Oversight Board agreed that a complete transformation of PREPA was necessary, which meant placing management of the transmission and distribution in private hands, and opening up the generation market to private competition.

PREPA's fiscal plan provides a roadmap for creating a new power sector for Puerto Rico that will: (i) provide lower-cost, clean electricity below 20 c/kWh, (ii) rebuild and maintain a modern, reliable, resilient grid, (iii) implement operational efficiencies to lower cost and improve service, and (iv) establish a fiscally responsible entity. The fiscal plan for PREPA also provides the framework for the myriad negotiations and processes that must occur for the successful transformation of PREPA. It includes a set of aspirational rate and reliability targets, and outlines transformation processes that can no longer be delayed, such as near-term investments in restoration, generation and resiliency; the scope and focus of federal funding; and the funding and/or size of transition charge available for restructuring debt and pension liabilities.

The fiscal plan also highlights the need for regulatory reform because a strong, independent, well-funded, professional regulator modeled on best practice regulatory structures employed in the United States is essential to any successful transformation of PREPA. That regulator will also oversee the development of a new Integrated Resource Plan ("IRP"), which will help define the optimal generation mix on the Island. In addition, the fiscal plan outlines the ultimate transformation transaction, which is currently underway and will bring about a concession of PREPA's transmission and distribution system, and privatization of its generation assets. The Oversight Board is tracking each of these critical processes and their interdependencies, noting and addressing any developments that put the goals of the transformation at risk and offering guidance on redirection as warranted.

VI. Debt Investigation

On September 1, 2017, the Special Investigation Committee of the Oversight Board engaged an independent investigator to carry out its mandate under Section 104 of PROMESA to conduct a

comprehensive investigation and review of the factors contributing to Puerto Rico’s fiscal crisis, Puerto Rico’s debt issuances, related disclosure and selling practices, Puerto Rico’s use of proceeds from debt offerings, and how Puerto Rico’s debt practices compare to the debt practices of states and large municipal jurisdictions.

To date, the independent investigator has collected a substantial volume of data and interviewed over 100 witnesses, including former governors of Puerto Rico; regulators who have in the past studied and proposed policy changes regarding Puerto Rico debt offerings; dozens of current and former senior officials and employees, including both career and political appointees, across multiple Puerto Rico administrations from the Government Development Bank for Puerto Rico, the Puerto Rico Department of the Treasury and the Puerto Rico Department of Justice; executives at various public corporations that issued debt; analysts from the ratings agencies; attorneys and other outside professionals who advised issuers and underwriters of Puerto Rico debt; investment bankers from institutions that underwrote Puerto Rico bond offerings; bondholders who invested in Puerto Rico securities; and other stakeholders. In addition, during the course of its investigation, the independent investigator has consulted with, and, as appropriate, solicited input from, the Retiree Committee and Official Committee of Unsecured Creditors in the Title III proceedings; various Puerto Rico and United States federal agencies and regulators; and the public.

At the conclusion of the investigation, the Oversight Board will publish the independent investigator’s final report, which will include an analysis of the historical and more recent macroeconomic and political factors contributing directly and indirectly to Puerto Rico’s fiscal crisis, the Puerto Rico municipal bond issuance process, and the legislative efforts to restructure the debt, in addition to its investigative findings, policy recommendations, and identification of potential claims and matters for regulatory attention.

VII. Recovery Plan

On February 9, 2018, Congress passed the “Bipartisan Budget Act of 2018,” which appropriated significant funds for disaster relief and recovery and required that the Governor, with support and contributions from various federal agencies and the Oversight Board, produce an economic and disaster recovery plan (the “Recovery Plan”) that defines the priorities, goals, and outcomes of the recovery effort. Congress specified that the plan be based on an up-to-date damage assessment and include the following sectors: housing; economic issues; health and social services; natural and cultural resources; governance and civic institutions; electric power systems and grid restoration; environmental issues; and other infrastructure systems.

Congress also required that the Oversight Board certify by August 8, 2018 that the Recovery Plan is “consistent with the purpose set forth in Section 101(a) of PROMESA,” which states that the Oversight Board “is to provide a method for a covered territory to achieve fiscal responsibility and

access to the capital markets.” As of the date of this Annual Report, the Oversight Board has not received the Recovery Plan from the Governor, and therefore has been unable to begin its review to determine whether to certify the Recovery Plan as satisfying the requirement that it is consistent with the purpose of PROMESA.

VIII. Title V Critical Projects Process

The Revitalization Coordinator restarted the Critical Projects Process in the aftermath of Hurricanes Irma and Maria. After hiring the requisite personnel, retaining local firms for additional support, and overhauling the project submission website, the Revitalization Coordinator was able to create a substantial pipeline of projects. At its peak, the Critical Projects Process received 40 different projects with a net investment value in excess of \$8.4 billion dollars.

One of the most critical factors in determining the success of any project is the engagement and support of the Government. To this end, the Revitalization Coordinator has dedicated substantial time and resources to coordinating with and learning from various agencies, offices, and commissions within the Government.

The Oversight Board designated “Viewpoint at Roosevelt,” a public housing development funded with federal funds, its first Critical Project. This project is expected to provide both critically needed housing (over 130 housing units) as well as increase ridership in the local rail system because it is located in a “public transport corridor.”

IX. Section 204 Legislative Review

Consistent with Section 204(a), the Oversight Board receives and analyzes all new legislation that is signed into law by the Government. This review process focuses on determining whether legislation is significantly inconsistent with the applicable fiscal plan, and is based in part on a report that the Government generates for each legislation.

Rather than wait for legislation that is inconsistent with the fiscal plan to be adopted, the Oversight Board tries to alert the Government of potentially problematic legislation before it becomes law. Accordingly, where possible, the Oversight Board does not rely on the Section 204 process to identify or take action with respect to legislation that is inconsistent with the fiscal plan.

X. Section 204 Contract Review

In November 2017, the Oversight Board established a policy pursuant to Section 204(b)(2) of PROMESA to require prior Oversight Board approval of contracts with an aggregate value of \$10 million or more that would be entered into by the Commonwealth of Puerto Rico or any covered

instrumentality. The objectives of this policy are to promote market competition and ensure that the government contracts are consistent with the applicable certified fiscal plan. Accordingly, the Oversight Board focuses its review on whether the contract is consistent with the fiscal plan and in the case of disaster aid spending, provide observations regarding the eligibility for federal funding and/or reimbursement.

During the last fiscal year, the Oversight Board received and reviewed 41 submissions composed of 76 individual contracts, totaling over \$5 billion. A substantial number of these contracts concerned Puerto Rico's reconstruction efforts after Hurricanes Irma and Maria, including (i) construction and repair of the power grid, (ii) debris removal, hauling, processing, and disposition, and (iii) grant management services, which are to provide assistance with managing federal disaster funding disbursement and reimbursement requirements. Additionally, the Oversight Board reviewed several contracts for various public agencies that covered a range of services from software licensing, to health insurance plan agreements, to professional services agreements. At the conclusion of each contract review, the Oversight Board publishes its responses and observations on its website.

The Oversight Board also established a contractor certification requirement as part of its contract review policy. All parties submitting contracts for approval under the policy are required to certify, among other things, that no fee sharing or undue government influence has occurred in connection with the procurement, negotiation, or execution of the contract. Moreover, the Oversight Board has included in the fiscal plan a requirement for the text of all government contracts to be made public on the Office of the Comptroller's website by September 30, 2018.

XI. Section 207 Debt Transaction Approvals

In December 2017, the Oversight Board established a policy pursuant to Section 207 of PROMESA to require prior Oversight Board approval of any debt transaction to be entered into by the Commonwealth of Puerto Rico or any covered instrumentality. The objectives of this policy are to promote fiscal prudence and ensure that the debt transactions are consistent with the applicable certified fiscal plan.

During the last fiscal year, the Oversight Board approved a variety of debt transactions. The most significant debt transaction was the debtor-in-possession loan from the Commonwealth to PREPA at a time when PREPA's operations were at a substantial risk of shutting down without emergency liquidity support. As part of this loan approval, the Oversight Board secured significantly most robust reporting requirements from PREPA to create more transparency into its cash management and operations. The Oversight Board also approved a loan from the Commonwealth to PRASA and insisted that the money be used in part to pay outstanding liabilities that PRASA owed to PREPA for electric service and to the pension fund for pay-go obligations. Finally, the Oversight

Board also approved the liquidation of guarantees that the GDB or its subsidiaries issued to private developments and the refinancing of certain loans that the Department of Housing and Urban Development issued to the municipalities of Camuy and San Lorenzo.

XII. Section 208(c) Cash Flow Report

Pursuant to Section 208(c), the Oversight Board, when feasible, is required to report the amount of cash flow available for the payment of debt service on all debt that is subject to a stay or moratorium under PROMESA. At this time, it is not feasible for the Oversight Board to make such a determination because it depends to a large extent on the completion of the bank accounts investigation, which, as described above, is ongoing.

XIII. Section 103(d) Federal Agencies Assistance

On January 17, 2018, the Chair of the Oversight Board requested assistance from the following federal departments and agencies pursuant to Section 103(d):

- Department of Energy
- Department of Treasury
- Department of Health and Human Services
- Department of Transportation
- Department of Education
- Department of Agriculture
- Department of Commerce
- Department of Housing and Urban Development
- Environmental Protection Agency
- General Services Administration
- Office of Management and Budget
- National Credit Union Association
- New York Federal Reserve

The Oversight Board received responses from the Department of Energy, Department of the Treasury, the Department of Health and Human Services, the Department of Transportation, the Department of Education, the Department of Commerce, the General Services Administration, the Office of Management and Budget, the National Credit Union Association, and the New York Federal Reserve. Most of the department and agencies indicated their willingness to work with the Oversight Board, but were unable to provide dedicated resources at the time.

Recommendations to the Federal Government

The Oversight Board strongly supports the Federal Government's swift actions to provide disaster relief funding for Puerto Rico in light of the destruction caused by Hurricanes Irma and Maria. The funding is welcome, deserved, and much needed by the U.S. citizens living in Puerto Rico. However, the disaster relief funding is by no means a long-term solution to Puerto Rico's long standing structural problems. This additional federal funding will provide a cushion of time within which Puerto Rico must continue the hard work of making the necessary structural changes, reforms and adjustments that will allow the Island to reverse the over decade long negative growth trend of the Puerto Rican economy, such that Puerto Rico can achieve fiscal balance, restructure the debt to sustainable levels, and return to capital markets.

Recommended Actions

Separate from disaster relief funding, the Oversight Board continues to believe that the Commonwealth's recovery and fulfillment of PROMESA's objectives will be significantly aided by the Federal Government's support in the following key Executive and Legislative areas:

I. Medicaid and Medicare

Legislate a long-term Medicaid program solution to mitigate the drastic reduction in federal funding for healthcare in Puerto Rico that will happen next year. Although Congress has provided Puerto Rico with additional Medicaid funding to finance Mi Salud (the state-run insurance program) at 100 percent Federal Medical Assistance Percentages (FMAP) for two years, this is not a long term or sustainable solution for Puerto Rico's healthcare crisis. It is important to provide fair treatment to the residents of Puerto Rico, to ensure the stability of the Island's healthcare system, and to avoid further outmigration. Currently, over 40% of the residents of Puerto Rico live under the federal poverty line and more than 45% of Puerto Ricans received their health coverage through the Commonwealth's Mi Salud, a higher proportion than the 50 states and D.C.

Amend federal law so that Medicare beneficiaries in Puerto Rico are automatically enrolled in Medicare Part B with the option to opt out of coverage, the same way their counterparts in every state and other territory are treated.

Provide fair and equitable treatment to residents of Puerto Rico in all Medicare programs. Residents of Puerto Rico pay the same level of Medicare taxes as mainland residents, but the Island receives substantially lower payments in Medicare programs.

II. Tax Provisions to Promote Economic Development

The U.S. Tax Reform amended the U.S. Tax Code to provide new international tax and base erosion rules for income generated by foreign subsidiaries (commonly referred to as “CFCs”) of U.S. parent companies. These new rules apply to CFCs operating in any part of the world, including Puerto Rico.

CFCs operating in Puerto Rico are crucial to Puerto Rico’s economy and are the main tax revenue generators for the Government of Puerto Rico. The new international tax and base erosion rules of the U.S. Tax Code should be framed in a manner that will help Puerto Rico, as a U.S. territory, retain the current CFC base and to favorably compete with foreign jurisdictions in attracting new investments, and to comply with the fiscal plan.

The U.S. Tax Code includes new Opportunity Zone (“OZ”) rules to promote investment in certain designated areas in the U.S., including Puerto Rico. The OZ rules offer tax incentives to investors that invest in an OZ Fund. The tax incentives are tied to the time investors hold their investments in an OZ Fund and certain adjustments to the “tax basis” of their investment.

The OZ rules are a unique opportunity for Puerto Rico because the entire Island qualifies as an OZ. However, the Island’s structural challenges caused by Hurricanes Irma and Maria and financial difficulties will require the OZ rules to include special provisions to increase Puerto Rico’s attractiveness for investments. For example, since Puerto Rico is currently in a reconstruction and development stage the rules should (a) provide special rules for property acquired from the Puerto Rico Government, (b) extend the time in which an OZ Fund must invest in Puerto Rico, (c) provide special basis rules for investors that invest in a Puerto Rico OZ Fund, and (d) reduce the holding period applicable to an investment in a Puerto Rico OZ Fund.

Recommend that Congress explore ways to minimize the challenges and maximize the opportunities of extending an Earned Income Tax Credit to residents of Puerto Rico.

III. Infrastructure, Housing, and Transportation

Remove regulatory burden inhibiting cargo commerce between Puerto Rico, the mainland, and international markets to establish Puerto Rico as a regional logistics hub for air cargo by supporting waivers for the Century of Aviation Reauthorization Act. Current law prohibits foreign civil aircraft from exchanging cargo in the United States unless the aircraft is specifically authorized to do so or the exchange occurs in Alaska. This change would apply air cargo regulation to Puerto Rico in the same way that it applies to Alaska, thus allowing foreign civil aircraft to stop in Puerto Rico and exchange cargo with other air carriers.

Eliminate the Electronic Export Information filing requirement for goods shipped between the mainland and Puerto Rico.

Direct relevant agencies to support bankable infrastructure projects through reduced red tape, targeted investments, and increased access to credit e.g. supporting monetization of toll credits, and to keep Puerto Rico top-of-mind for infrastructure funding and improvements.

Allow authorities to use disaster relief funds to cover land surveys, land titles, and any other taxes or fees associated with property transfer.

Encourage the U.S. Army Corps of Engineers and ENLACE to finalize the Project Partnership Agreement for the Caño Martín Peña project.

IV. Benefits Reform

Extend the full federal Child Tax Credit to residents of Puerto Rico to allow otherwise eligible families in Puerto Rico with one child or two children to claim the additional child tax credit. This legislative change will provide the same treatment to families in Puerto Rico with one child or two children that is currently provided to Island families with three or more children and to families across the 50 states and the District of Columbia. The Congressional Task Force Report includes estimates claiming that this proposal could benefit about 355,000 newly-eligible families and 404,000 newly-eligible children in Puerto Rico, with an average credit for all Puerto Rico families of \$770, which will help reduce child poverty on the Island.

Work with the Government of Puerto Rico to institute a work requirement for able-bodied participants aged 18-59 to receive the Nutritional Assistance Program (NAP), which is Puerto Rico's largest welfare program. This work requirement should be established in accordance with the Commonwealth Fiscal Plan. In general, working-age Supplemental Nutrition Assistance Program beneficiaries on the mainland must register for work, cannot turn down a job if offered, and may be required by the state to attend education or work training classes.

Direct the Health Resources and Services Administration to utilize the Puerto Rico Community Survey when allocating funds to Puerto Rico under the Maternal, Infant, and Early Childhood Home Visiting Program.

V. Education and Employment

Ask the Department of Labor to partner with the Commonwealth to enable the expansion of apprenticeship programs to link education with marketable skills and employment in order to ensure the workforce is prepared for the jobs of the future.

Encourage Department of Homeland Security to carve out a lower investment floor for EB-5 visas relative to states to tailor visa programs to Puerto Rico's needs.

Encourage the National Science Foundation to collaborate with all possible stakeholders to avoid funding loss for the Arecibo Observatory and to increase science and education-focused operations.

VI. Manufacturing

Establish a Manufacturing USA institute in Puerto Rico to equip Puerto Rico with the partnerships and resources necessary to continue developing as a world renowned pharmaceutical manufacturing center and to become a global biotech innovation hub.

VII. Small Business

Provide greater flexibility for Small Business Administration Programs to help Puerto Rico's small business owners during the prolonged economic crisis. This includes many of the recommendations included in the Congressional Task Force Report: enact legislation to increase the guaranty rate and require a separate subsidy calculation for 7(a) loans made in Puerto Rico; consider reducing the small business contribution and increasing the Certified Development Companies (CDC) contribution; consider increasing that aggregate limit for the Microloan program in the case of intermediaries located in Puerto Rico; authorize an intermediary in the Microloan program to use more than 25 percent of its SBA-provided technical assistance grants on pre-loan assistance if the intermediary provides at least 25 percent of its loans to small firms in Puerto Rico; establish a contracting preference for small businesses in Puerto Rico with respect to federal contracts performed in Puerto Rico; and require the SBA to make an annual FAST partnership grant to a Puerto Rico grantee, and to waive the local matching requirement.

VIII. Tourism

Request that the Secretary of Commerce appoint at least one member who has special expertise on tourism in Puerto Rico to the United States Travel and Tourism Advisory Board.

IX. Financial Institutions

Request that the Community Development Financial Institutions Fund website update its maps to represent visually that Puerto Rico is eligible for its programs, encourage it to increase the number of Community Development Financial Institutions in Puerto Rico, ask that it assist FDIC-insured banks in Puerto Rico regarding the Bank Enterprise Award program, and encourage it to appoint

an individual with experience and expertise in Puerto Rico to the Community Development Advisory Board.

X. Statistics

Direct the Census Bureau, Bureau of Labor Statistics, Bureau of Justice Statistics, Bureau of Economic Analysis, National Center for Education Statistics, National Center for Health Statistics, and Substance Abuse and Mental Health Services Administration to include Puerto Rico in their respective programs and to collect and publish data for Puerto Rico on the same basis as the states to the greatest extent possible.

Assign funds to the Census Bureau to perform a Special Census of Governments for Puerto Rico for 2017, that would provide much needed up-to-date comparable financial information for credit markets.

Support for Pending Legislation

The Oversight Board supports the following non-exhaustive list of pending legislation:

- H.R. 2488 – Puerto Rico Small Business Assistance Act of 2017
- H.R. 2531 – Puerto Rico Medicare Part B Equality Act of 2017
- H.R. 3226 – Supplemental Security Income Equality Act of 2017
- H.R. 3472 – Puerto Rico Air Cargo Industry Empowerment Act
- H.R. 6211 – Puerto Rico Data Collection Equality Act of 2018
- S. 2873 / H.R. 5975 – Puerto Rico Economic Empowerment Act of 2018
- H. AMDT. 564 – An amendment numbered 81 printed in Part A of House Report 115-650 to require a study and data collection of the air cargo traffic in the Caribbean region.
- H. AMDT. 618 – An amendment numbered 15 printed in House Report 115-679 to require the Secretary of Agriculture to provide an extension of study on comparable access to Supplemental Nutrition Assistance for Puerto Rico.

Conclusion

As established in last year's Annual Report, the Oversight Board continues to believe that any amendments to PROMESA would distract and detract from the Government of Puerto Rico and the Oversight Board doing the hard work of balancing the Commonwealth's budget, restructuring the Commonwealth's obligations, and turning around the Commonwealth's economy.

The Oversight Board looks forward to working with the Federal Government on the aforementioned areas.

Budget for the Oversight Board

Below is a summary of the Oversight Board’s financial report for fiscal year 2018. For more information, please see Annex A.

	General Fund
	(In thousands)
REVENUES:	
Contributions from territorial government	\$ 60,000,000
Interest income	9,000
	60,009,000
EXPENDITURES:	
Payroll and other related costs	2,969,000
Rent and other office costs	318,000
Purchased services	3,093,000
Transportation and travel costs	540,000
Professional services	52,378,000
Materials and supplies	18,000
Equipment purchases	55,000
Other expenditures	457,000
	59,828,000
EXCESS OF REVENUES OVER EXPENDITURES AND NET CHANGE IN FUND BALANCE	181,000
FUND BALANCE - July 1, 2017	348,000
FUND BALANCE - June 30, 2018	\$ 529,000

The notes to the forecasted financial statement are an integral part of this statement.
This forecasted financial statement has not been audited, reviewed or compiled and
no assurance is provided on it.

Other Activities by the Oversight Board

The Oversight Board held five public meetings, a public hearing on the Government's bank accounts, and four listening sessions with various stakeholders as part of the fiscal plan development and evaluation process. The Oversight Board also held numerous meetings with stakeholders, including creditors, professional organizations, businessmen, union leaders, UPR students, mayors, legislators, NGOs, former governors, and others, as part of its ongoing work.

Members and executive staff of the Oversight Board met regularly and exchanged frequent correspondence with Government officials regarding the development, certification, and implementation of the fiscal plans and budget. In addition, members and executive staff of the Oversight Board held meetings and exchanged correspondence with U.S. Government and Congressional officials regarding Hurricanes Irma and Maria and updates on the Oversight Board's work in Puerto Rico. The Oversight Board also appeared before Congressional panels and submitted letters for the record in connection with various Congressional hearings.

Finally, the members and executive staff of the Oversight Board also held periodic media roundtables, press conferences, interviews and press calls to continually inform the public and key stakeholders regarding the Oversight Board's work.

Below is a representative sample of key events, speaking engagements, public meetings, and hearings for the members and staff of the Oversight Board:

- FOMB Chair Op-ed *A new path* in El Nuevo Día (7.5.17)
- FOMB designates Noel Zamot as Revitalization Coordinator (7.23.17)
- FOMB Public Board Meeting in SJ (8.4.17)
- FOMB Executive Director Op-ed *A new paradigm* in El Nuevo Día (8.9.17)
- Title V Critical Project Process Website Launch (8.23.17)
- FOMB Executive Director Keynote Speech at Puerto Rico is the Answer Forum in SJ (8.24.17)
- FOMB Chair Keynote Speech at the Puerto Rico Association of General Contractors Convention in Fajardo (8.25.18)
- FOMB Chair Keynote Speech at the Puerto Rico United Retailers Center (CUD) in Rio Grande (8.25.17)
- FOMB Revitalization Coordinator Op-ed *A powerful tool* in El Nuevo Día (8.9.17)
- Hurricane Irma hits Puerto Rico (9.4.17)
- FOMB Executive Director Keynote Speech at Dear Fiscal Board Speaker Series Forum in SJ (9.9.17)
- FOMB Debt Investigation Committee designates Kobre & Kim to begin independent investigation on Puerto Rico's debt (9.13.17)
- FOMB Member Skeel talk at Northwestern Univ. School of Law (9.19.17)

- FOMB Chair Op-ed *Make Puerto Rico grow again* in Caribbean Business (9.21.17)
- FOMB grants \$1B Reapportionment Authority to Puerto Rico Government (9.22.17)
- FOMB designates Noel Zamot as Chief Transformation Officer (CTO) (10.25.17)
- FOMB Public Board Meeting in SJ (10.31.17)
- FOMB Chair Keynote Speech at American Enterprise Institute Forum in DC (11.6.17)
- Public Testimony of FOMB Executive Director and Revitalization Coordinator at U.S. House Natural Resources Committee Hearing (11.7.17)
- Public Testimony of FOMB Revitalization Coordinator at U.S. Senate Energy & Natural Resources Committee Hearing (11.14.17)
- FOMB Fiscal Plan Public Listening Session in SJ (11.16.17)
- FOMB Fiscal Plan Public Listening Session in SJ (11.30.17)
- FOMB Fiscal Plan Public Listening Session in NY (12.4.17)
- FOMB Public Board Meeting in NY (12.5.17)
- FOMB Public Board Hearing on Government Accounts in SJ (1.19.18)
- FOMB General Counsel panel participant in “Rebuilding Puerto Rico: Strategies, Partners and the Role of the Oversight Board”, New York City Bar Association (1.22.2018)
- FOMB Chair Keynote Speech at Second PROMESA Conference in SJ (1.31.18)
- FOMB PREPA Public Listening Session in NY (2.1.18)
- FOMB Chair Keynote Speech at Puerto Rico Manufacturers Association Forum in SJ (2.9.18)
- FOMB Chair Keynote Speech at the 2018 Puerto Rico Investment Summit in SJ (2.12.18)
- FOMB Executive Director Keynote Speech at Pharmaceutical Industry Association Convention in SJ (2.22.18)
- FOMB Executive Director Keynote Speech at Certified Public Accountants Association Forum in SJ (3.15.18)
- FOMB Executive Director Keynote Discussion at University of Chicago Institute of Politics Speaker Series in Chicago (4.4.18)
- FOMB Executive Director Panel Discussion at University of Notre Dame Hesburgh Center for International Studies on Sustainable Development in South Bend (4.5.18)
- FOMB Chair Op-ed regarding Pension Reform in El Nuevo Día (4.9.18)
- FOMB Public Board Meeting in SJ for Fiscal Plans Certification (4.19.18)
- FOMB Public Board Meeting in SJ for Fiscal Plans Certification (4.20.18)
- FOMB Member Skeel talk at Univ. of Chicago School of Law sponsored by the Federalist Society (4.23.18)
- FOMB Member Skeel talk at Univ. of Puerto Rico Law Review Symposium (5.4.18)
- FOMB Executive Director Keynote Speech at P.R. Association of Financial Analysts Luncheon in SJ (5.4.18)
- FOMB Chair Keynote Speech at United Group of Automobile Importers Luncheon in Carolina (5.23.18)

- FOMB P.R. Fiscal Plan Recertification by Unanimous Written Consent (5.30.18)
- FOMB Chair Carrión and Member Biggs participation in Heritage Foundation Forum on Puerto Rico in DC (6.21.18)
- FOMB Fiscal Plans Recertification by Unanimous Written Consent (6.29.18)
- FOMB P.R. and Instrumentalities FY19 Budgets Certification by Unanimous Written Consent (6.30.18)

Conclusion

The Oversight Board acknowledges the long road ahead for Puerto Rico but is resolute in fulfilling its mission of helping Puerto Rico to achieve fiscal responsibility, regain access to capital markets, restructure its outstanding debt, and return to economic growth.

The Oversight Board is grateful to the governmental agencies and legislative staff, special interest groups, and members of the public, both on the mainland and in Puerto Rico, for the information and insight they've provided during the past year and looks forward to strengthening these relationships in furtherance of the Oversight Board's mission in the upcoming year.

Financial Oversight and Management Board for Puerto Rico



Budgetary Comparison Schedule For Year Ended June 30, 2018 (Annex A)

FINANCIAL OVERSIGHT AND MANAGEMENT BOARD OF PUERTO RICO
FOR THE YEAR ENDED JUNE 30, 2018

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COMMONWEALTH OF PUERTO RICO
FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO

BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
FOR THE YEAR ENDED JUNE 30, 2018

	Final Budget	Actual Amounts in Budgetary Basis (Forecast)	Variance Favorable (Unfavorable)
	<u> </u>	<u> </u>	<u> </u>
REVENUES:			
Contributions from territorial government	\$ 60,000,000	\$ 60,000,000	\$ -
Other	9,800	88,712	78,912
	<u>60,009,800</u>	<u>60,088,712</u>	<u>78,912</u>
Total revenues	<u>60,009,800</u>	<u>60,088,712</u>	<u>78,912</u>
EXPENDITURES:			
Payroll and other related costs	3,289,599	2,235,190	1,054,409
Rent and other office costs	189,380	166,722	22,658
Purchased services	2,556,915	2,201,486	355,429
Transportation and travel costs	1,483,265	1,088,604	394,661
Professional services	51,979,546	42,552,360	9,427,186
Materials and supplies	13,082	11,463	1,619
Equipment purchases	148,896	93,069	55,827
Other expenditures	349,117	339,144	9,973
	<u>60,009,800</u>	<u>48,688,038</u>	<u>11,321,762</u>
Total expenditures	<u>60,009,800</u>	<u>48,688,038</u>	<u>11,321,762</u>
EXCESS OF REVENUES OVER EXPENDITURES	<u>\$ -</u>	<u>\$ 11,400,674</u>	<u>\$ 11,400,674</u>

The notes to this budgetary comparison schedule are an integral part of this schedule.

This budgetary comparison schedule has not been audited, reviewed or compiled and no assurance is provided on it.

Fiscal year has not been closed, and forecast for expenditures include accruals for unbilled services.

FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO

NOTES TO BUDGETARY COMPARISON SCHEDULE – GOVERNMENTAL FUND FOR THE YEAR ENDED JUNE 30, 2018

2

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

On June 30, 2016, the Financial Oversight and Management Board for Puerto Rico (the Oversight Board) was established by the bipartisan Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") in Public Act 114 - 187 of the 114th Congress to address the economic crisis in Puerto Rico and to provide a method for Puerto Rico as a covered territory to achieve fiscal responsibility and to restore access to the capital markets.

The Oversight Board is tasked with working with the Government of Puerto Rico to create the necessary foundation for economic growth and to restore opportunity to the people of Puerto Rico. The Oversight Board consists of seven members appointed by the President of the United States and an ex-officio member appointed by the Governor of Puerto Rico.

Section 107(a) of PROMESA establishes that a budget should be adopted for each fiscal year of operations and shall be submitted to the President, the House of Representatives Committee on Natural Resources and the Senate Committee on Energy and Natural Resources, the Governor, and the Legislature in accordance with section 107(a) of the Act. In accordance with Article VIII of the Oversight Board Bylaws, as amended, the Chair shall propose for each fiscal year an annual budget for the Oversight Board no later than one month before the beginning of the fiscal year, which upon an affirmative vote of a majority of the members then serving shall be adopted as the annual budget of the Oversight Board, except that the budget for the initial fiscal year shall be proposed and adopted pursuant to a schedule as determined by the Chair.

The Oversight Board shall, from time to time as it deems necessary, notify the Governor and the Legislature its funding requirements as set forth in section 107(b) of PROMESA.

A. Budgetary Accounting

The Oversight Board's budget is prepared in accordance with a statutory basis of accounting, which is not in accordance with accounting principles generally accepted in the United States of America (US GAAP). Revenue is generally recognized when cash is received and expenditures are generally recorded when the related expenditure is incurred or encumbered. Amounts required for the settlement of claims and judgments against the Oversight Board, and certain other liabilities are not recognized until they are encumbered or otherwise processed for payment. Specifically, certain liabilities for the year ended June 30, 2018 have been accrued for purposes of this budgetary comparison schedule.

Under statutory basis of accounting, the Oversight Board uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of allocated resources as deductions from the allocation prior to actual expenditure. In the general fund, encumbrance accounting is a significant aspect of budgetary control.

The Oversight Board funds do not have a legally mandated budget.

B. Budgetary Control

Formal budget integration is employed as a management control device during the fiscal year for the general fund. The annual budget for the fiscal year ended June 30, 2018 was **\$60,000,000**.

FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO

NOTES TO FORECASTED STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE – GOVERNMENTAL FUND (CONTINUED)
FOR THE YEAR ENDING JUNE 30, 2018

3

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY (CONTINUED)

B. Budgetary Control (Continued)

The Oversight Board's revenues are established by PROMESA in Section 107, which states that on the 5th day of each month the Governor of Puerto Rico shall transfer or cause to be transferred the greater of \$2,000,000 or such amount as shall be determined by the Oversight Board to an account under the exclusive control of the Oversight Board from a dedicated funding source and without any legislative appropriations of the territorial government. The contributions from territorial government presented are those estimated by the Oversight Board as sufficient to cover all expenditures for its operations for the fiscal year ended June 30, 2018 using the zero-based budgeting method.

As also established by PROMESA in Section 107, if the Oversight Board determines in its sole discretion that any funds transferred exceed the amounts required for the Oversight Board's operations, any such excess funds shall be periodically remitted to the territorial government.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For US GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.