

PROMESA: The Good, the Bad and the Ugly

How PROMESA Should Work!

How PROMESA Is Working!

How Financial Recovery Can Be Obtained!

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I. The Gathering Storm of Puerto Rico's Financial Distress: To Understand the Purpose, Function and Desired Result of PROMESA, It Is Important to Understand the Systemic Causes of Puerto Rico's Financial Distress

A. Puerto Rico's financial problems did not begin with the Great Recession of 2007:

1. The systemic roots of Puerto Rico's financial problems did not begin in the 21st century but go back to inchoate systemic issues which have their beginnings in the 20th century:
 - (a) Merchant Marine Act of 1920 – Puerto Rico's import costs are at least double those of neighboring island countries due to this Act (a/k/a Jones Act) which encourages all goods transported by water to be carried by U.S. flagships and taxes those foreign flagships that carry cargo between the U.S. mainland and Puerto Rico.

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- (b) Puerto Rico's constitutional changes loosen balanced budgets and debt limits – In 1952, amendment allowed balancing budgets with non-revenue sources such as federal aid and, in 1961, amended debt limit to percent of revenue from percentage of property.
- (c) Repeal of Section 936 IRC tax credits – In 1996, federal legislation sunsetted Section 936 benefits over a 10-year period effective 2006. Section 936 tax credits are attributed to encourage many capital-intensive businesses to chose to relocate to Puerto Rico providing new jobs and accompanying economic benefits.

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- (d) Unequal treatment under Medicare and Medicaid, SSI, EITC and CTC – Puerto Rico claimed to lose billions due to 50 years of unequal treatment of Puerto Rico under Medicaid, Medicare, 40 years of unequal treatment under Supplemental Security Income ("SSI") and Earned Income Tax Credit ("EITC") programs and nearly 20 years of unequal treatment under the Child Tax Credit ("CTC").

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2. By 2006 and the adverse effects of the repeal of Section 936, Jones Act, unequal treatment under Medicaid, Medicare, SSI, EITC, CTC, Puerto Rico had a budget crisis and a short shutdown of government:
 - (a) In hindsight, PROMESA would have been more helpful and less drastic if it or something similar was initiated in 2006 rather than ten years later. On May 1, 2006, with a lack of agreement on a budget, 45 government agencies including public schools closed leaving 95,762 people temporarily unemployed.

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- B. Part of the Puerto Rico solution to the 2006 budget crisis was to borrow funds to help balance the budget – a fatal budgetary policy:
1. In 2006, Puerto Rico public debt was approximately \$40 billion with a public debt per capita of \$10,666.66 and public debt as a percentage of GDP of 45.82% compared to \$72 billion of public debt in 2015 (the eve of PROMESA) with a public debt per capita of \$20,727.38 (nearly double 2006) and public debt as a percentage of GDP of 69.83% (24 percentage points more than 2006). The average for state and local governments in U.S.A. is \$5,663.88 which is $\frac{1}{4}$ the debt per capita of Puerto Rico.
 2. Public debt is not the cause of financial distress of a government, it is a symptom of a systemic problem.

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C. After 2006, Puerto Rico's financial situation took a steeper downward path into financial distress:

1. GNP declined since 2007 – 2016 by 14% and employment in Puerto Rico fell by 250,000 to less than one million.
2. Unemployment rate in Puerto Rico was 12.1% in October 2016 with a 23% drop in persons employed since December 2006 (from 1,277,599 to 987,606).
3. Labor participation rate of Puerto Rico in 2016 was 40%, two-thirds of the 63% level on the U.S. mainland.
4. Puerto Rico's population declined by 10% in the last ten years, about 1% per year.

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5. Poverty rate for Puerto Rico in 2015 was 45.1% of Puerto Rico residents compared to the U.S. mainland average of 14.7%.
6. Economic Activity Index (payroll employment, electric power generation, cement sale and gasoline consumption) dropped from 160.4 in August of 2005 to 124.1 in August 2016.

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- D. There are systematic causes of Puerto Rico's financial distress separate and apart from the devastation caused by Hurricane Maria that PROMESA and any recovery plan must address:
1. Counter past economic downturn with economic stimulation and development – With the repeal of Section 936 and exit of corporate and individual taxpayers, with the accompanying loss of tax revenues, there has been no real replacement or long-term economic development strategy to expand business in Puerto Rico, attract new business to Puerto Rico, thereby providing new, good jobs for Puerto Rico's population and attracting a significant increase in population and taxpayers.

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2. Correction of adverse federal policies that cost Puerto Rico billions such as the permanent repeal of the Jones Act, elimination of any inequalities in Medicare, Medicaid, SSI, EITC and CTC – Federal assistance in programs to develop new commerce and economic stimulation (such as encourage increased business activity and support manufacturing opportunities, high tech, green tech, creation of new energy generation and strategy for the short-term and long-range economic development plan by Puerto Rico that its creditors can buy into).

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3. Solving the tax collection problem through identification and implementation of new or increased tax sources along with increasing efficiency of tax collection – The exploration of new tax policies that would stimulate economic development and new tax sources that do not adversely affect such economic development efforts. Further dealing with subterranean economy and deficiencies in tax collection methods.
4. Reverse the stigma of financial distress by improving financial creditability in the capital markets – It would be counter-productive to have the result of any recovery plan be less access and increased borrowing cost for Puerto Rico. Accordingly, steps should be taken to assure that the recovery plan will increase market access and lower cost of borrowing both short-term and long-term. This can be done by following established, best practices of government accounting, administrative budgeting and financing.

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5. Treatment of outstanding public debt by PROMESA process must be perceived by the market as fair – As a result of the widespread devastation of the island caused by Hurricane Maria, holders of the public debt of the Commonwealth and other related issuers are faced with an inability to pay situation. While federal assistance to the island will be forthcoming, it is unlikely that this assistance will take the form of a bailout of outstanding public debt. Some members of Congress, while rejecting any notion that such debt will be cancelled by executive order, have suggested that the PROMESA process, to be discussed in the next few slides, should be allowed to play out for such debt but that revenues to debtholders would be reduced from those proposed by the fiscal plan. It will be important that the ultimate resolution of the outstanding public debt be perceived as fair and not arbitrary under the circumstances.

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E. Proposed further response to Hurricane Maria to address the need to rebuild Puerto Rico's infrastructure and stimulate its economy:

1. The United States has a history of helping those who have endured events that caused human suffering. The United States has a long and proud history of helping others in time of natural disasters, to reduce human suffering going back to the earthquake that hit Venezuela in 1812 during the War of 1812. This aid by the United States continued on in helping others during times of natural and manmade disasters such as earthquakes in Sicily and Calabria in 1908, floods in France in 1911, volcanic eruption on Martinique and St. Vincent in 1902, the Marshall Plan for Europe and the rebuilding of Japan after World War II, civil strife in Cypress in 1964-1965, Jordan in 1970, the Seven Day War in the Mideast in 1967, and more recently, the tsunami in the Indian Ocean in 2004 striking 14 countries, the earthquake in Haiti in 2010, and the earthquake, tsunami and nuclear disaster in Japan in 2011 to name a few. Accordingly, it should be more compelling to provide the rebuilding of Puerto Rico by the Federal Government and U.S. Congress, since it is a U.S. Territory and its inhabitants are U.S. citizens. Further, U.S. Congress has the mandate and power under the Constitution to dispose of and make needful rules and regulations respecting U.S. territories (U.S. Constitution, Article 14, Section 3).

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2. First stop human suffering and develop a Marshall-type plan for Puerto Rico's governmental services and infrastructure – The first immediate action is to assure the health, safety and welfare of the citizens of Puerto Rico with food, water, medical services, governmental service and infrastructure all to a level deemed acceptable. This is a Marshall-type plan for Puerto Rico for services and infrastructure (roads, water, sewer, electricity, etc.) at a level that citizens find will justify wanting to remain there and can attract new citizens and businesses that want to be there and expand their businesses in Puerto Rico. This will create new, good jobs that produce additional tax revenues that provide the revenues needed for a recovery.

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3. Develop a long-range economic development strategy for Puerto Rico to elevate Puerto Rico's business opportunities and roles in the Caribbean – There should be a long-range economic recovery plan for Puerto Rico which is implemented at the same time or in coordination with the Marshall-type plan that establishes viable and desirable services and infrastructure at the appropriate level as noted above. This economic development plan should provide assured liquidity for continued uninterrupted governmental operations and any necessary bridge financing in coordination with the implementation of the “Marshall-type plan.”
 - Puerto Rico as the center of commerce to the Caribbean. The economic recovery plan should consider making Puerto Rico (which means Rich Port) the key point of commerce for the Caribbean.

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Numerous islands have been affected by the hurricanes in the Caribbean and Puerto Rico could be the port and the location where all relief and all commercial activity is focused as the staging and coordinating center. This allows a coordinated effort and allows Puerto Rico to be elevated to a key role for the Caribbean.

- **Puerto Rico as the banking hub for the Caribbean.** Part of this would include establishing Puerto Rico as the center of commerce for the Caribbean for banking, shipping and processing assembly of goods from foreign manufacturers for distribution in the Caribbean and possibly Central American and other locations.

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Also, legislation by Congress and the Commonwealth could provide for financial banking services to be the U.S.A. equivalent of the Cayman Islands for specialty financings and investment vehicles. This would facilitate Puerto Rico become the banking center for the Caribbean like London has been for Europe.

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- Puerto Rico as the major foreign trade zone for the Caribbean.

Also, as part of the economic recovery plan, the whole island of Puerto Rico should become a foreign trade zone (a free trade zone) where equipment, goods and parts manufactured in foreign countries can be shipped to Puerto Rico duty-free and processed, assembled or manufactured with only limited duties on the finished product. Such actions would stimulate additional business activity and the benefits of the jobs multiply for financial, shipping and manufacturing new jobs [directed (the new jobs created by the economic policy), indirect (jobs created for good and services to support the direct job) and induced (jobs created by salaries spent for goods and services by those with the direct and indirect jobs)]. This would significantly increase employment and the labor participation rate which is presently 40% compared to 63% for the U.S.A. on average and as well as reduce the poverty rate for Puerto Rico of over 45%, by far the highest compared to the U.S. states average of 14.7%.

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4. Congress can enact or adjust laws, rules and regulations to promote Puerto Rico's economic development and to remedy those that purport to treat Puerto Rico unfairly:
 - **Congress was the constitutionally mandated duty to promote economic development for Puerto Rico.** The Territorial Clause of the U.S. Constitution provides “Congress shall have power to dispose of and make all needful rules and regulations respecting the territory or other property belonging to the United States.” (U.S. Constitution, Article IV, Section 3).

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- **Actions Puerto Rico and Congress should consider taking.** Based on this, Congress should examine existing legislation that could be modified to assist Puerto Rico in its effort to resolve its financial and infrastructure crisis. The Jones Act that requires foreign flag vessels that stop in the U.S.A. continental ports and Puerto Rico to pay a tariff increasing the cost of goods for Puerto Rico should be repealed for Puerto Rico. The Commonwealth and others have pointed out a needed review of federal laws, rules, regulations and policy to ensure appropriate fairness compared to the treatment of states and others. Puerto Rico contends it has lost billions of dollars due to unequal treatment under Medicaid and Medicare for 50 years, under Supplemental Security Income (“SSI”), Earned Income Tax Credit (“EITC”) programs for over 40 years and under the Child Tax Credit (“CTC”) program for nearly 20 years. The lack of stimulus for economic and business development in Puerto Rico following the repeal of Section 936 tax exemption for U.S. companies, the claimed disproportionate burden of Medicaid and social programs, the need for effective tax reform and efficient collection methods suggest the consideration of review and, where needed, modification of existing laws that have impeded Puerto Rico’s economy.

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5. The path forward for Puerto Rico, its citizens, businesses and creditors:
 - **The need for consensus by all the parties.** Citizens, taxpayers, individual and corporate and creditors of Puerto Rico should support the above proposal for economic recovery plan since it is the economic growth and success of Puerto Rico that is the means by which additional tax revenues will be raised by creating new taxpayers and jobs that provide the funds to pay obligations like debt and to fund governmental services and infrastructure at the desired level. There should be a consensus by creditors, taxpayers and citizens on this.

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- **Recovery plan for all – leave no one behind.** There is no substitute for the practical ability to be paid from a recovery plan that maximizes value and recoveries to the extent reasonable and reinvests in Puerto Rico to ensure continual operations and sufficient tax revenues to reasonably pay off its creditors based on what can be paid.

If there is no money, there is no payment no matter the rights or priorities. All the rights legally possible do not necessarily translate into payment of public debt or assurance of funding of essential services and needed infrastructure at an acceptable level.

II. The Enactment of PROMESA and Its Provisions

- A. The impending fiscal crisis – By 2016, the serious financial problems of the territory of Puerto Rico had reached the tipping point of a crisis:
1. As noted above, for years, Puerto Rico, faced with a failing economy, financed operations with the issuance of tax-exempt bonds that the rating agencies had now deemed junk.
 2. Puerto Rico had ever increasing costs of essential services and needed infrastructure improvements including an expensive health insurance program for low-income people without providing for a means of paying for it.
 3. Further, public pensions, including those for teachers, judges and general employees, were largely unfunded.

II. The Enactment of PROMESA and Its Provisions

4. Those who could left the island for better economic opportunities resulting in a loss of over 250,00 residents/taxpayers since 2006.
5. There was little or no significant economic investment or growth on the island, and the government could not meet its debt obligations and also provide basic governmental services.
6. Schools were closing and hospitals were in precarious positions.

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- B. The PROMESA solution – In an effort to save Puerto Rico from imminent economic collapse, particularly because of the \$1.9 billion bond debt payment due July 1, 2016, Congress enacted the Puerto Rico Oversight, Management and Economic Stability Act ("PROMESA"), which became law on June 9, 2016:
1. Origins of PROMESA – PROMESA was intended to be an eclectic mixture of past mechanisms used to resolve financial distress of governments such as the Municipal Assistance Corporation for New York City in 1975, the Pennsylvania Intergovernmental Cooperative Authority for Philadelphia in 1999, and the Financial Responsibility and Management Assistance Authority for the District of Columbia in 1995. PROMESA took what it considered the best attributes of these and other mechanisms and incorporated them into PROMESA.

II. The Enactment of PROMESA and Its Provisions

2. Its goals – The principal goal of PROMESA was to provide the Commonwealth of Puerto Rico with an opportunity and framework to stabilize the economy, restructure its debt, and develop a realistic budget and develop a recovery plan. The Act also provided a short-term stay on litigation and other efforts to collect debt that admittedly was in default. The Act encouraged consensual resolution with creditor groups under Title VI where creditor groups can collectively agree with Puerto Rico as to a resolution and drag the non-consenting holders along which then could be a foundation, if all issues were not resolved with all creditors classes, for a plan of adjustment under a Title III proceeding. At the same time, the Act did not enact limitations on the Commonwealth's exercise of its governmental powers.

II. The Enactment of PROMESA and Its Provisions

3. The Act is structured into seven sections or titles.
4. Title I – Establishment and organization of Oversight Board:
 - (a) Title I establishes a Financial Oversight and Management Board (the "Oversight Board") of seven voting members appointed by the President of the United States with the advice and consent of the United States Senate.
 - (b) The Oversight Board is not compensated.
 - (c) A majority vote of the Oversight Board is required for the approval of a fiscal plan or budget, to cause an act by the Puerto Rico legislature not to be enforce, or to approve an infrastructure project.

II. The Enactment of PROMESA and Its Provisions

- (d) The Oversight Board is to carry out the purposes of PROMESA and may hire staff and counsel as necessary. Its powers include the power to:
- hold hearings,
 - issue subpoenas, obtain data and creditor information,
 - enter into contracts, enforce laws and certify voluntary creditor agreements
 - supervise to balance budgets,
 - prohibit public sector strikes, and
 - implement an efficient taxation system.

II. The Enactment of PROMESA and Its Provisions

5. Title II – Responsibilities of Oversight Board: Stop the Bleeding and Bridge to Financial Stability:
 - (a) Title II of PROMESA sets forth the responsibilities of the Oversight Board:
 - approving a fiscal plan covering at least five years,
 - approving the budget that complies with the fiscal plan,
 - making legislative recommendations to the Governor and Legislature of Puerto Rico to promote financial stability and economic growth,
 - consenting to debt restructuring, and
 - intervening in litigation against Puerto Rico.

II. The Enactment of PROMESA and Its Provisions

6. Title III – Adjustment of debts:

- (a) Title III creates a procedure for the adjustment of the debt of the Commonwealth of Puerto Rico akin in certain respects to the procedure under Chapter 9 of the Bankruptcy Code.
- (b) PROMESA incorporates a number of sections of the Bankruptcy Code, including:
 - Section 301 in PROMESA incorporates by reference provisions of the Bankruptcy Code into Title III namely sections 902 (special revenues), 922 (automatic stay and exception for special revenues), 923 (notice of commencement of case), 924 (list of creditors), 925 (effect of claim list), 926 (avoiding powers), 927 (limitation on recourse), 928 (post petition effect of security interest), 942 (modification of plan), 944 (effect of confirmation), 945 (continuing jurisdiction and closing the case) and 946 (effect of exchange of securities before the date of filing of the petition), and

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- Other sections of Chapter 9 are repeated with some modification in specific sections of PROMESA such as 903 (reservation of power of state to control municipalities–Section 303 of PROMESA), 904 (limitation on jurisdiction and power of the court–Section 305 of PROMESA), 929 (municipal leases–Section 311 of PROMESA), 941 (filing plan–Section 312(b) of PROMESA), 942 (modification of plan section 942 incorporated by reference and set forth in Section 313 of PROMESA), 943 (confirmation–Section 314 of PROMESA).
- (c) The Oversight Board may file a voluntary petition under Title III in the United States District Court for the District of Puerto Rico.
- (d) The Oversight Board prosecutes the case on behalf of the Commonwealth of Puerto Rico.

II. The Enactment of PROMESA and Its Provisions

7. Differences between Chapter 9 and PROMESA Title III:
 - (a) The Oversight Board has a key role in the proceeding and prosecutes Puerto Rico's case (Section 315) unlike Chapter 9 where the municipality as debtor represents itself.
 - (b) The plan of adjustment must be the one approved by the Oversight Board (Section 315) unlike Chapter 9 where the debtor municipality develops and files the plan without need of approval from another entity.

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- (c) There is a mechanism for professionals to be paid during the interim and at the end of the case – compensation for representing the debtor, the Oversight Board, creditor committee(s) appointed by the court or a trustee to pursue avoidance causes of action (Section 316) unlike Chapter 9 where there are no provisions to compensate professionals. This Section 316 could conflict with Section 305 of PROMESA that provides the court does not have jurisdiction over revenues of Puerto Rico without the consent of the Oversight Board.

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- (d) The presiding judge shall be a federal district court judge to conduct the proceedings (Section 308), an Article III judge, while under Chapter 9, the judge presiding by reference would be bankruptcy judge (Article I).
- (e) Appeals of the Title III court rulings are to be taken like an appeal of a district court ruling (Section 306) to the Federal Courts of Appeals for the First Circuit unlike a Chapter 9 where appeals are made to the district court or to the Bankruptcy Appellate Panel (BAP) first before going to the federal appellate court.

II. The Enactment of PROMESA and Its Provisions

8. Title IV miscellaneous provisions, automatic stay, and inter-debtor property transfer protection:
 - (a) Included in the miscellaneous provisions are sections that assure the right of Puerto Rico to determine its future political status (Section 402), deal with minimum wage for certain workers (Section 403), review of certain labor regulations applicability to Puerto Rico (Section 404), impose automatic stay upon enactment to prevent preferential creditor action and encourage consensual resolution (Section 405), create a Congressional task force regarding economic growth in Puerto Rico (Section 409), and implement new reporting requirements of the comptroller general relating to Puerto Rico's debt and financial condition (Section 409 and 410).

II. The Enactment of PROMESA and Its Provisions

9. Title V – Puerto Rico infrastructure revitalization:
 - (a) PROMESA provides for a revitalization coordinator to review proposed projects for revitalizing the infrastructure of the Commonwealth of Puerto Rico (Section 502):
 - Critical project reports including expedited permitting process and prioritization of action items subject to Oversight Board approval (Section 503).
 - Expedited review and action by any federal agency including as to federal grants and loans (Section 505).
 - Expedited judicial review of any claim related to infrastructure revitalization.
 - (b) This Title V also has provisions governing expediting critical projects required because of an emergency affecting the physical infrastructure and threatening public health and safety. This may provide a vehicle to address emergency infrastructure improvements (water, electricity, roads, etc.) given the devastation of Hurricane Maria.

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10. Title VI – Creditor collective action:

- (a) PROMESA provides for a method of debt restructuring outside of Title III.
- (b) The Oversight Board is required to divide the Commonwealth of Puerto Rico's creditors into separate pools based upon the nature of the debt and at least one pool for each issuer.
- (c) Each pool after delivery of adequate information would then vote on a qualifying modification to the debt owed, which would become binding if supported by a two-third majority of outstanding principal in the pool that has voted, provided at least a majority of the outstanding principal of that pool has voted and the district court approves the resolution.

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Note: If 51% of the outstanding amount of debt affected vote and two-thirds of those voting approve the restructuring, it is possible that about 34% of all outstanding amount of debt of a class of creditors could direct a resolution and drag 66% of the outstanding amount of debt along.

- (d) The District Court in Puerto Rico has the power to order any dissenting creditors to accept the qualifying modification.
- (e) This collective action by creditor groups has no real precedent in government debt restructuring in the U.S. but a collective action clause is common in other foreign country debt agreements.

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11. Title VII – The sense of Congress:

- (a) The sense of Congress is to establish permanent, pro-growth fiscal reforms that feature a free flow of capital between the United States and the Commonwealth of Puerto Rico.

III. How PROMESA Should Work

- A. Accurate information – Obtain accurate information on Puerto Rico's ability to pay and nature and extent of the indebtedness of Puerto Rico and its covered territorial entities:
 - 1. Nature and extent of creditor claims – The Oversight Board by requests or subpoena can obtain complete information from creditors on their respective claims (documents, purchase price, how long they held the debt, and related relationship or agreements among creditors).

III. How PROMESA Should Work

2. Determining the ability to pay current expenses, liabilities and creditor groups – Through budgets submitted by Puerto Rico to the Oversight Board for approval, the development of a fiscal plan by Puerto Rico for approval by the Oversight Board, and information as to revenue, current expenses, and liabilities, the ability to pay should become transparent. To the degree information is not complete or forthcoming, the Oversight Board can subpoena it. As approved, the budget and fiscal plan are shared with the creditors and other parties in interest to help having everyone be on the same financial page.

III. How PROMESA Should Work

- B. Encourage consensual resolution – The structure of PROMESA is to encourage consensual resolution of disputes under Title VI prior to any resort to the more costly and less efficient Title III debt adjustment proceeding:
1. Consent of all creditors of a debt pool is not required – After the Oversight Board works with Puerto Rico to develop a going forward budget and fiscal plan for creditors' consideration, the basic financial information should be available to the various creditor groups to have intelligent discussion of how much is available and the ability to pay and limitations of any debt restructuring. If creditors believe more revenue or consideration can be provided by Puerto Rico or other debtor entities, there is no bar to creative and constructive proposals and possible financial alchemy.

III. How PROMESA Should Work

2. Fair resolutions are facilitated under Title VI – The benefit of the collective action of creditors of a debt pool is that they can realistically evaluate proposals and make proposals for restructuring and, if successfully negotiated with Puerto Rico and the other respective debtors, can effectively have the restructuring binding on all creditors by having the proposal as agreed to with Puerto Rico communicated and voted on by the affected creditors. If two-thirds of over a majority of principal amount of the debt voting approve, then after notice it can be taken to the district court for approval to determine compliance with the requirements of Title VI. This voting criteria, at a minimum, requires as little as 34% of the outstanding amount of the debt pool of creditor class that could vote to approve a resolution if only 51% of the outstanding debt voted. If the proposal is fair and reasonable as determined by the court, it can be binding on all such affected creditors of that pool. Each of these deals are a basic building block toward a global settlement with all creditors.

III. How PROMESA Should Work

3. Only after a significant effort to obtain Title VI collective action agreements should a Title III debt adjustment procedure be considered – Only after all affected creditors have had an opportunity to negotiate a fair and reasonable resolution should there be any effort to consider a Title III debt adjustment proceeding. The goal is a holistic restructuring proposal for all creditors to come together and help determine what is sustainable and affordable as a fair resolution.

III. How PROMESA Should Work

4. Title III is the last resort – Title III should be the last resort after all effort to mediate and resolve issues between creditor groups and with the debtor are resolved. While priorities and rights of creditors have importance, the ability to pay and methods of maximizing value are key to understanding the realistic and probable range of recovery and preventing legal meltdown.
- C. Title III should only be pursued after exhaustion of Title VI efforts – If consensual resolution is not possible for all creditors, then a Title III plan of adjustment becomes necessary.

III. How PROMESA Should Work

- D. Before filing Title III proceedings, Puerto Rico should have proposed budgets and a fiscal plan approved by the Oversight Board – By the time it is determined that consensual resolution under Title VI is not possible, Puerto Rico should have prepared its budgets and fiscal plan for approval by the Oversight Board and the Oversight Board should have approved them (possibly after modification suggested by the Oversight Board). These actions provide the financial basis for a Title III plan of adjustment and the parameters for the appropriate adjustment of debt.

III. How PROMESA Should Work

- E. Plan of adjustment of debt is also to be feasible and in the best interests of creditors if it is sustainable and affordable in the long term, resolves creditor disputes and also stimulates the economy – The plan of debt adjustment to be feasible must be in compliance with a sustainable and affordable budget and fiscal plan as approved by the Oversight Board that stimulates the economy and economic benefits, provides sufficient funding of essential services and necessary infrastructure improvements as encouraged by PROMESA under Title IV, V and VII. If the plan of adjustment does not assure the long-term survival of Puerto Rico (including funding of essential services and infrastructure improvements) how could it be in the "best interest of creditors" who are only paid over the long term?

III. How PROMESA Should Work

F. Summary of relevant duties of the Oversight Board:

1. Role and goal of Oversight Board – One of the first responsibilities of the Oversight Board is to assist Puerto Rico in developing a fiscal plan and budgets that can be approved and certified by the Oversight Board. The fiscal plan, budgets and any plans of adjustment as approved by the Oversight Board should provide a method of delivering the goals of achieving fiscal responsibility and access to the capital markets.
2. Oversight Board makes the decision to commence Title III proceedings – Under Section 304 of PROMESA, the Oversight Board, assuming five members of the Oversight Board are in agreement that certain conditions exist, can commence a case under Title III of the Act to restructure its debt, a process akin to U.S. Bankruptcy protection.

III. How PROMESA Should Work

3. The Oversight Board to act for Puerto Rico in the Title III proceedings and limitations on the court's jurisdiction – The Oversight Board (and not elected officials) is to serve as the Commonwealth's representative in the Title III proceeding and is to file the petition and plan of adjustment and to be responsible for restructuring negotiations:
 - (a) Title III of PROMESA incorporates many provisions of the United States Bankruptcy Code, including the automatic stay provisions and the protections included in the municipal bankruptcy provisions for holders of debt secured by a pledge of special revenues.

III. How PROMESA Should Work

- (b) Title III specifically states that it does not limit or impair the power of the territory in the exercise of its political or governmental powers, including expenditures for such exercise (Section 303 of PROMESA and Section 903 of Chapter 9).
- (c) However, Title III does not permit the discharge of obligations arising under federal police or regulatory laws, including laws relating to the environment or public health or safety (Section 304 of PROMESA).

III. How PROMESA Should Work

- (d) Unless the Oversight Board consents or the plan of adjustment so provides, the court may not, by any stay, order or decree in the Title III proceeding, interfere with:
 - Any of the political or governmental powers of the debtor;
 - Any of the property or revenues of the debtor; or
 - The use or enjoyment by the debtor of any income-producing property (PROMESA 305, Section 904 of Chapter 9).
- 4. The Oversight Board shall certify and file a plan of adjustment for the debts of Puerto Rico which the Oversight Board may modify any time before confirmation so long as the plan as modified meets the requirements of Title III.
- 5. The Oversight Board may certify a plan of adjustment only if it determines, in its sole discretion, that it is consistent with the applicable certified fiscal plan.

III. How PROMESA Should Work

G. PROMESA – Title III principles of debt adjustment:

1. PROMESA court's limited jurisdiction – The court under PROMESA cannot:
 - (a) Limit or impair the territory's laws and legislative mandates as they existed at the time of passage of PROMESA including as to the exercise of the territory and territorial instrumentalities of their political or governmental powers including as to expenditures (Sections 201(b)(1)(M) and (N) and 303 of PROMESA).
 - (b) The court may not by any stay, order or decree in the Title III proceeding interfere with any political or governmental powers, property or revenues or use or enjoyment of income producing property of Puerto Rico or its instrumentalities in Title III proceeding UNLESS the Oversight Board consents.

III. How PROMESA Should Work

Query: What about claims and adversary actions where the Puerto Rico laws mandate payment (like COFINA sales tax revenues to COFINA bonds or the purported pledge of revenues by PREPA, HTA, PRASA, *et al.*, to their bondholders) or the Oversight Board has not consented to the court hearing the matter and there is mandated payment as required by the provision of the constitution and statutory laws?

- (c) Section 303(3) of PROMESA provides "unlawful executive orders that alter, amend, or modify rights to holders of any debt of the territory or territorial instrumentalities or that divert funds from one territorial instrumentality to another or to the territory shall be preempted by this Act."

Query: The power of the court to divert funds mandated by territory statutes or constitution to pay debts of Puerto Rico and its public corporations COFINA, HTA, PREPA, PRASA, etc.?

III. How PROMESA Should Work

2. Protection of public debt that is subject to special revenues and statutory liens under a PROMESA's Title III proceeding:
 - (a) What is a statutory lien:
 - Basic Provisions for a Statutory Lien. Generally, the statute from which the statutory lien arises:
 - Contains language such that the force and effect of the statute creates the interest in the dedicated revenues or proceeds to pay the debt without need of further action by the issuing governmental entity.
 - May also provide for the priority of payment, a first lien or provision that the dedicated pledged revenues can only be used to pay the debt or in the order specified in the statute or authorizing documents.

III. How PROMESA Should Work

- May also provide an intercept or segregation of the revenues or require a governmental entity or officer to collect and pay over to a special account or to the bond trustee.
- Additionally, some states provide by statute that the state or local government, upon issuing debt pursuant to a specific state statute, automatically grants a lien (dedicated revenues or proceeds only to be used to pay the debt prior to any other use) on specified property, proceeds or tax revenue for the payment of the debt so incurred.
- The granting by a local government pursuant to a local ordinance, without more, is unlikely to give rise to a statutory lien. Note: Statutes are legislative enactments by the state, and ordinances are legislative enactments by municipalities and are not statutes and cannot give rise to a statutory lien.

III. How PROMESA Should Work

- As established in the Orange County Chapter 9 bankruptcy, *In re County of Orange*, 189 B.R. 499, 503 (C.D. Cal. 1995), and other related case law, the federal bankruptcy court cannot interfere with the constitutional or statutory mandated payments and the dedicated revenues pledged to pay public debt. Sections 303 and 305 of Title III (Sections 903 and 904 of the Bankruptcy Code) require the payment mandated by statute be paid by those specifically dedicated revenues as they are collected and not used for any other purposes.

III. How PROMESA Should Work

- (b) What is a special revenues pledge? Section 902(2) of the Bankruptcy Code, which is incorporated into Title III of PROMESA, defines special revenues as:
- (2) "special revenues" means—
- (A) receipts derived from the ownership, operation, or disposition of projects or systems of the debtor that are primarily used or intended to be used primarily to provide transportation, utility, or other services, including the proceeds of borrowings to finance the projects or systems;
 - (B) special excise taxes imposed on particular activities or transactions;
 - (C) incremental tax receipts from the benefited area in the case of tax-increment financing;

III. How PROMESA Should Work

- (D) other revenues or receipts derived from particular functions of the debtor, whether or not the debtor has other functions; or
 - (E) taxes specifically levied to finance one or more projects or systems, excluding receipts from general property, sales, or income taxes (other than tax-increment financing) levied to finance the general purposes of the debtor.
- (c) What are the benefits of statutory liens and special revenues?
- Create predictable priorities in Chapter 9 and Title III. These types of financings are intended to create predictable priorities in Chapter 9 and Title III so municipal bond market participants can be protected by a predictable result.

III. How PROMESA Should Work

- Outside Chapter 9 and Title III, payment is enforceable. Outside of a Chapter 9 and Title III proceeding, participants would be protected through enforcing payment by writ of mandamus or other remedies and the fact that a governmental officer must comply with the mandate of state law or suffer the penalties.
- Assured payment is the intended result. In Chapter 9 and Title III, there is intended to be established priority and assurance of payment so that governmental bodies suffering from temporary illiquidity would have access to the municipal bond market with a dedicated source of payment that would survive Chapter 9. (See legislative history of 1988 Amendments to the Bankruptcy Code regarding solving the dilemma of the City of Cleveland in 1978. See Sections 201(b)(1)(M) and (N), 305 and 305 of PROMESA.)

III. How PROMESA Should Work

- (d) How are special revenues to be treated in Title III?
- Timely payment as the pledge of special revenue provides. A special revenue pledge is to be unaltered in a Chapter 9 proceeding, and the timely payment of the pledged revenues by the municipality is required by the Bankruptcy Code. Section 922(d) of the Bankruptcy Code is incorporated into Title III and provides the automatic stay is not applicable to special revenues.
 - Obligation and payment to be unimpaired. Special revenues were intended by the 1988 Amendments to the Bankruptcy Code to be unimpaired in Chapter 9 and the debt holders intended to receive the benefit of the bargain, so the same should be applicable to Title III proceedings.

III. How PROMESA Should Work

- Case law supports the unimpaired status. This unimpairment was respected in the Chapter 9 proceedings of the *Sierra Kings Health Care District* Chapter 9 (Eastern District of California), *Jefferson County, Alabama* (Northern District of Alabama) *Stockton, California*, and *Detroit, Michigan* (for those who continued to hold Water and Sewer Revenue Bonds, the case reaffirmed the unaltered status and timely payment of special revenue pledges in a Chapter 9 proceeding).

III. How PROMESA Should Work

- No termination of special revenues, lien or revenues but the issue of payment of necessary operating expenses from project or system revenues. Section 928(a) of the Bankruptcy Code incorporated into Title III provides that the lien on pledged special revenues is not terminated upon the commencement of a Title III action but if the pledged special revenues are revenues of a system or project, such as fees or rates from a public utility, then special revenues are subject to the necessary operating expenses of the project or system (Section 928(b)). Revenues of the system and project that are special revenues cannot be used for purposes not connected to the system or project. If the special revenues are revenues specifically pledged to pay the public debt but are not revenues of the system or project and cannot be used for other purposes, such as for operating expenses of the system or project, by the express terms of the operative agreements of the financing, then the payment of special revenues to public debt is not subject to the necessary operating expenses requirement of § 928(b).

III. How PROMESA Should Work

(e) How are statutory liens treated in Title III?

- Statutory lien is to be unaltered and timely paid. A statutory lien should remain unaltered in a Title III proceeding, and there is a continuing right to be timely paid after the filing of a Title III action given the language of Sections 303 and 305.
- Chapter 9 cases recognize the unaltered treatment. Such unimpairment was recognized in the Chapter 9 proceedings of *Orange County, California* in 1994 (delay in payment due to appeal and reversal of Bankruptcy Court as to effect of a statutory lien) and the *Sierra Kings Health Care District* Chapter 9 in 2009 (relating to General Obligation Bonds).

III. How PROMESA Should Work

- Analysis of statutory liens by state. A number of states have statutes containing statutory lien provisions. See e.g., Rhode Island, California, Colorado, Idaho, Louisiana and New Jersey (Municipal Qualified Bond Act). Statutory lien legislation is pending in Michigan (HB 4495), Nebraska (LB 72) and Illinois (HB 2584). See the 50 State Survey in the second edition of "Municipalities in Distress?" for breakdown of statutory lien categories for further analysis).

III. How PROMESA Should Work

3. Other protections of public debt contained in Title III:
 - (a) No preferences for payment of bonds and notes prior to filing of Title III proceeding. Any payment or refunding of notes or bonds cannot be the subject of a Section 547 action to avoid the transfer and clawback the payment within the preference period under Section 926(b) of the the Bankruptcy Code incorporated into Title III.

III. How PROMESA Should Work

- (b) Special revenues have a forced election to pledged revenues with no other recourse to the debtor in Title III. Under Section 927 of the Bankruptcy Code incorporated into Title III, a special revenues creditor has recourse to the special revenues and is deemed to have elected not to assert a recourse claim against a Title III debtor under Section 1111(b) of the Bankruptcy Code. For this reason, there can be no substitution, delay or impairment of the special revenues payments as required to be made by the Bankruptcy Code and Title III from the pledged and dedicated special revenue stream or other use of special revenues.

III. How PROMESA Should Work

- (c) Government leases are not executory contracts or unexpired leases. Under Section 929 of the Bankruptcy Code, incorporated into Title III, a lease to Puerto Rico or its instrumentalities shall not be treated as an executory contract or unexpired lease by reason of its being terminated in the event the debtor fails to appropriate rent. In essence, the lease obligation is treated as debt with no discount under Section 502(b)(6) of the Bankruptcy Code or capable of rejection under Section 365 of the Bankruptcy Code.

III. How PROMESA Should Work

- (d) The plan of adjustment and implementation of the plan must comply with Title III provisions and the constitutional and statutory law of Puerto Rico. Under Section 314 of PROMESA (similar to Section 943 of the Bankruptcy Code), the plan and any actions to implement the plan must be consistent with Title III and the laws of Puerto Rico. Also, it must be feasible and in the best interest of creditors which means the plan is sustainable and affordable and provides for essential governmental services and necessary infrastructure improvements as encouraged by Title IV, V and VII, as noted above. The financial survival of the government is in the "best interest of creditors" since creditors are paid in the long term.

III. How PROMESA Should Work

H. PROMESA – Provisions for emergency situations:

1. Critical projects, designed to deal with an event or grave problem of deterioration in the physical infrastructure that threatens health and safety, are subject to an expedited permitting process.
2. This expedited process does not apply to any federal law, statute, or requirement.
3. Such project must include in its submission the availability of immediate private capital or other funds and whether Puerto Rico government funds will be necessary to complete and maintain the project.
4. Critical project subject to approval by the Oversight Board.

IV. How Has Title III of PROMESA Worked So Far?

A. Action of the Oversight Board and Puerto Rico under PROMESA and development of a fiscal plan:

1. Development of Puerto Rico's fiscal plan. On March 13, 2017, prior to the Title III filing, the Government of Puerto Rico submitted its Fiscal Plan for Puerto Rico. The Fiscal Plan anticipated that the central government would have enough available money to pay \$404 million of \$3,283 million of scheduled debt service or 12.3% in fiscal year 2018. The Puerto Rico Electric Power Authority ("PREPA"), the Puerto Rico Aqueduct and Sewer Authority ("PRASA"), the Children's Trust Fund and the Puerto Rico Housing Finance Authority ("PRHFA") were not included in the Fiscal Plan.

IV. How Has Title III of PROMESA Worked So Far?

2. Need to allocate specific payment to creditors in the fiscal plan. The Fiscal Plan did not attempt to allocate the cash flow available for debt service among the different debt instruments, but reported that total public sector debt totaled approximately \$74 billion.
3. Need to deal with public pension underfunding. Further, total pension liabilities were approximately \$49 billion.
4. Efforts to understand and assist Puerto Rico and creditors to reach consensual agreement. From December 2016 through March 2017, the Oversight Board and the Commonwealth of Puerto Rico met frequently with creditor representatives but no consensual restructuring was reached.

IV. How Has Title III of PROMESA Worked So Far?

5. Oversight Board approval of fiscal plan. On March 13, 2017, the Oversight Board certified an amended version of the Fiscal Plan, but creditors were not happy with the level of debt service. The amended version included the implementation of a furlough program and an overhaul of the public pension system.
6. Mediation efforts were made with little success. The Oversight Board and the Commonwealth began mediation on April 13, 2017, but no consensual agreement was reached. Government Development Bank (“GDB”) and PREPA did reach agreement with certain of their creditors groups. Both the Governor of Puerto Rico and the Oversight Board have approved the GDB debt restructuring. The restructuring must also be approved by Judge Swain.

IV. How Has Title III of PROMESA Worked So Far?

7. Automatic stay prior to Title III. Section 405 of PROMESA imposed an automatic stay on litigation and other preferential actions against the Commonwealth of Puerto Rico, for a period from enactment with extension which expired May 1, 2017.
8. Filing of Title III proceeding. With the expiration of the stay, many creditors filed suit against the Commonwealth leading to the Title III filing in the U.S. District of Puerto Rico on May 3, 2017.

IV. How Has Title III of PROMESA Worked So Far?

B. The filing of cases under Title III to be jointly administered and public debt:

1. Cases filed under Title III. The principal Title III cases originally filed by the Oversight Board:
 - (a) The Commonwealth of Puerto Rico,
 - (b) Puerto Rico Sales Tax Financing Corporation (COFINA), a statutory instrumentality of the Commonwealth created to issue bonds secured by the assignment of certain sales tax revenues,
 - (c) Puerto Rico Highways and Transportation Authority, and
 - (d) Employees Retirement System of the Government of the Commonwealth of Puerto Rico.

IV. How Has Title III of PROMESA Worked So Far?

2. Appointment of a federal district court judge to hear the cases. The Chief Judge of the United States Supreme Court named Federal District Court Judge Laura Taylor Swain to preside over the cases. Judge Swain has referred certain matters to Magistrate Judge Judith G. Dein.
3. Joint administration of the cases. The judge originally issued orders providing that the Title III cases listed in (1.) above be jointly administered for procedural purposes only and not affecting any substantive consolidation of the cases. Further, the dockets for these cases, for administrative purposes only, are to be maintained on the CM/ECF system of the United States Bankruptcy Court for the District of Puerto Rico.

IV. How Has Title III of PROMESA Worked So Far?

4. Appointment of certain official committees:
 - (a) On June 15, 2017, the acting U.S. Trustee for Region 21 (Puerto Rico) appointed an Official Committee of Unsecured Creditors for the Commonwealth of Puerto Rico. No public debt bondholders, indenture trustees or bond insurers were appointed to the Committee. This may possibly be due to claims that such public debt is secured by special revenues, statutory lien or constitutional mandated priority that would make the public debt claims dissimilar in nature of claims from the unsecured creditors. Two public employee unions and five trade creditors were appointed to the Unsecured Creditors Committee. On August 11, 2017, the court denied a motion of bondholders to reconstitute the Official Committee of Creditors and add bondholder representatives.

IV. How Has Title III of PROMESA Worked So Far?

- (b) Also, on June 15, 2017, the acting U.S. Trustee for Region 21 (Puerto Rico) appointed an Official Committee of Retirees in the Commonwealth of Puerto Rico case. The Committee consists of nine individual retirees. On September 8, 2017, the court denied a motion of the Ad Hoc Puerto Rico's Municipalities' Committee to appoint an Official Committee for Municipalities. The Court found belated arguments that Government Development Bank ("GDB") is the alter ego of the Commonwealth to be unfounded since they are separate, legal entities pursuant to the applicable statute and GDB is not a Title III debtor and the municipalities claim to be creditors of GDB.

IV. How Has Title III of PROMESA Worked So Far?

5. Administrative actions by the court in the Title III cases to facilitate consensual resolution with communication and input from creditors:
 - (a) On June 14, 2017, Judge Swain entered an Order designating a mediation team composed of five judges to conduct mediation of key matters and issues on creditor claims.
 - (b) An initial, confidential mediation meeting between certain mediation team members and parties in interest listed took place on July 12, 2017 in New York City. The meeting was not open to the public or the media and participants were forbidden to bring any personal electronic devices or general purpose computing devices to the meeting.

IV. How Has Title III of PROMESA Worked So Far?

- (c) The court has approved the employment of Phoenix Management Services, LLC as Financial Advisor for the mediation team. Martha E.M. Kopacz, who was appointed by Judge Steven Rhodes to serve as his Independent Expert on the feasibility of the Plan of Adjustment for the City of Detroit, will be responsible for the Phoenix engagement in this matter.
- (d) Federal Rule of Bankruptcy Procedure Rule 9019 provides for compromise and settlement approved by the court within the zone of reasonableness given the likelihood of each of the respective parties prevailing on the merits. But, there could be objections by some affected creditors and assertion of their rights is permitted and any approval can be appealed.

IV. How Has Title III of PROMESA Worked So Far?

- (e) Title VI creditor actions should also be available if there is a solicitation with adequate information regarding the voting of creditors affected by a resolution to the affected creditors and the approval of the requisite percentage by creditors voting and district court approval. As noted above, this procedure in Title III may be viewed under some circumstances as similar to Title VI, but the standard for court approval under F.R.B.P. Rule 9019 is in the zone of reasonableness given the likelihood of success on the merits compared to the requirements of Title VI that the court find the resolution is in the best interest of creditors, feasible and consistent with the fiscal plan after favorable vote by affected creditors.

IV. How Has Title III of PROMESA Worked So Far?

6. Filing of PREPA Under Title III:

- (a) On July 2, 2017, the Oversight Board filed a Title III Petition for the Puerto Rico Electric Power Authority, PREPA.
- (b) PREPA had not been the subject of the Fiscal Plan referenced above for the Commonwealth. Rather, PREPA and its creditors, including certain bondholders, insurers and full-line lenders had spent several year negotiating the terms of a Restructuring Support Agreement regarding debt relief (PREPA believes it has over \$10 billion in liabilities, including \$8.3 billion principal amount of power bonds) and the recovery plan. The PREPA Revitalization Act was signed into law in February of 2016 and a Restructuring Order was issued by the Puerto Rico Energy Commission in June of 2016.

IV. How Has Title III of PROMESA Worked So Far?

- (c) According to the Oversight Board, the Restructuring Support Agreement left a number of material issues subject to further negotiation (how monoline insurers would provide required principal deferrals, the terms of new full line credit agreements, a revised electric rate structure) and the required validation proceedings were not completed.
- (d) On June 28, 2017, the Oversight Board denied certification of the Restructuring Support Agreement and did not grant authority to PREPA to invoke Title VI of PROMESA.
- (e) PREPA had a debt service payment due July 1, 2017. On July 2, the Title III case for PREPA was filed. According to the Oversight Board, it and PREPA intend to continue pursuing consensual negotiations with PREPA's key stakeholders.
- (f) On October 6, 2017, the court entered an order providing that the PREPA case would be procedurally consolidated and jointly administered with the earlier Title III cases.

IV. How Has Title III of PROMESA Worked So Far?

- (g) A group of PREPA bondholders filed a motion to lift the automatic stay to allow movants to enforce their statutory right and right under the Bond documents to have a receiver appointed for PREPA following an event of default: the failure to comply with the rate covenant. The movants complain that the Oversight Board has not recognized the bondholders' right to increase rates found in the Bond Indenture and Puerto Rico statute. The Title III court denied the motion by an opinion and order dated September 14, 2017 holding that Section 305 of PROMESA prohibits the court from transferring control of PREPA's management and property to a receiver without the Oversight Board's consent. Further, even if the court had the power to grant the request, the court held that the appointment of a receiver to force a rate increase would impede the power of the Oversight Board. The bondholders have filed an appeal to the United States Court of Appeals for the First Circuit.

IV. How Has Title III of PROMESA Worked So Far?

- (h) Following criticism of PREPA's award of a \$300 million contract to a small Montana energy firm for work on the island's crippled electrical grid, the Oversight Board announced it would install an emergency manager at the utility. Since this would effectively remove control away from the Governor and PREPA's own board, it is expected that the Governor will resist this action by the Oversight Board. The Governor subsequently requested that PREPA cancel the contract. A motion was filed by the Oversight Board to confirm the appointment and authority of Noel Zamot as chief executive officer of PREPA reporting to the Oversight Board.

IV. How Has Title III of PROMESA Worked So Far?

7. Bond Insurers and others seek investigation of Puerto Rico's finances. National Public Finance, Assured Guaranty and others had filed motions seeking an order against the Oversight Board, the Commonwealth and the Puerto Rico Fiscal Advisory Authority permitting discovery pursuant to Bankruptcy Rule 2004 to determine the basis for the Fiscal Plan, if bondholders are being paid all that can be paid and if a plan of adjustment based upon the Fiscal Plan is confirmable. Following the devastation caused by Hurricane Maria, the viability of the Fiscal Plan generally will be revisited.

IV. How Has Title III of PROMESA Worked So Far?

8. Puerto Rico's principal public corporations. In connection with the filing, the Oversight Board described some of the Commonwealth of Puerto Rico's principal public corporations, which are potential debtors in Title III:
 - (a) Puerto Rico Highways and Transportation Authority (HTA) – created to assume responsibility for the construction and maintenance of roads and highways and related transportation facilities in Puerto Rico (filed);
 - (b) Puerto Rico Electric Power Authority (PREPA) – supplies substantially all the electricity consumed in the Commonwealth and owns all transmission and distribution facilities and most of the generating facilities that constitute Puerto Rico's electric power system filed;

IV. How Has Title III of PROMESA Worked So Far?

- (c) Puerto Rico Aqueduct and Sewer Authority (PRASA) – owns and operates Puerto Rico's public water supply and wastewater systems;
- (d) Government Development Bank (GDB) – historically, served as (i) fiscal agent, financial advisor, and reporting agent for the Commonwealth, its instrumentalities, and municipalities, (ii) an important source of financing for various Commonwealth entities, and (iii) the principal depository of the funds of the Commonwealth entities;
- (e) Puerto Rico Health Insurance Administration (PRHIA) – created to negotiate and contract for the provision of comprehensive health insurance coverage for qualifying (generally low income) Puerto Rico residents;

IV. How Has Title III of PROMESA Worked So Far?

- (f) Puerto Rico Medial Services Administration (PRMSA) – operates and administers certain centralized health services;
- (g) University of Puerto Rico (UPR) – the only public university in Puerto Rico;
- (h) Puerto Rico Integrated Transit Authority (PRITA) – created to integrate the mass transit services currently provided by HTA, MTA, and MBA;
- (i) Puerto Rico and Municipal Island Maritime Transport Authority (MTA) – operates ferry services between the Municipalities of San Juan and Cataño, and Fajardo, Vieques, and Culebra;
- (j) Metropolitan Bus Authority (MBA) – operates bus and paratransit services within Puerto Rico's metropolitan area;

IV. How Has Title III of PROMESA Worked So Far?

- (k) Puerto Rico Public Buildings Authority (PBA) – created to design, construct, administer, and provide maintenance to office buildings, courts, warehouses, schools, health care facilities, welfare facilities, shops, and related facilities leased to the Commonwealth or any of its departments, agencies, instrumentalities, or municipalities;
- (l) Puerto Rico Ports Authority (PRPA) – owns the major airport and seaport facilities in Puerto Rico;
- (m) Puerto Rico Industrial Development Company (PRIDCO) – created to promote economic development by stimulating the formation of new local firms and encouraging firms in the United States and foreign countries to establish and expand their operations in Puerto Rico;

IV. How Has Title III of PROMESA Worked So Far?

- (n) Puerto Rico Tourism Company (PRTC) – responsible for stimulating, promoting, and regulating the development of Puerto Rico's tourism industry;
- (o) Puerto Rico Infrastructure Financing Authority (PRIFA) – created to provide financial, administrative, consulting, technical, advisory, and other types of assistance to other public corporations, governmental instrumentalities, political subdivisions, and municipalities authorized to develop infrastructure facilities and to establish alternate means for financing those facilities;
- (p) Agricultural Enterprises Development Administration (ADEA) – created to provide a wide array of services and incentives to the agricultural sector;

IV. How Has Title III of PROMESA Worked So Far?

- (q) Puerto Rico Housing Finance Authority (PRHFA) – created to provide public and private housing developers with interim and permanent financing through mortgage loans for the construction, improvement, operation, and maintenance of rental housing for low and moderate-income families;
- (r) Puerto Rico Tourism Development Fund (TDF) – created to facilitate the development of Puerto Rico's hotel industry by working with private-sector financial institutions in structuring financings for new hotel projects and hospitality related projects;
- (s) Puerto Rico Development Fund – established to provide an alternate source of financing to private enterprises;

IV. How Has Title III of PROMESA Worked So Far?

- (t) Puerto Rico Public Finance Corporation (PFC) – established to provide agencies and instrumentalities of the Commonwealth with alternate means of meeting their financing requirements;
- (u) State Insurance Fund (SIF) – in charge of managing and regulating the Commonwealth workers' insurance system that covers occupational injuries, diseases, and deaths, to which all employers must be subscribed under law; and
- (v) Puerto Rico Sales Tax Financing Corporation (COFINA) – created, among other things, to raise money for the Commonwealth in exchange for the Commonwealth's transfer to COFINA of certain sales and use taxes filed.

IV. How Has Title III of PROMESA Worked So Far?

9. List of public debt of Puerto Rico and its instrumentalities. In connection with the Title III filing, the Oversight Board submitted to the court the debt summary that had been part of the Fiscal Plan.

IV. How Has Title III of PROMESA Worked So Far?

Summary of debt outstanding as of February 2017 (\$MM)

Issuers included in Fiscal Plan	Bond principal	CAB	Unpaid P&I ¹	Private Loans	Total Bonds & Private loans	Loans from GDBMFA Entities	Total Debt Service FY 17-19	DSRF Balance
GO	\$12,013	\$84	\$1,146	\$24	\$13,267	\$169	\$3,284	—
COFINA	11,425	6,155	—	—	17,580	—	2,121	—
HTA ²	3,983	135	6	—	4,124	1,734	997	101
PBA	3,980	—	117	—	4,097	182	782	6
GDB ^{3,4}	3,182	—	742	203	4,126	—	1,863	—
ERS	2,658	498	—	—	3,156	—	500	44
PRIFA ⁵	1,566	409	232	—	2,207	49	464	2
PFC	1,025	—	172	—	1,197	—	257	—
UPR ⁶	496	—	—	0	496	76	145	61
PRCCDA	386	—	—	—	386	145	91	9
PRIDCO	145	11	—	—	156	78	54	19
AMA	—	—	—	28	28	—	—	—
Other Cental Gov't Entities	197	—	29	413	639	3,975	—	—
Total	\$41,056	\$7,293	\$2,444	\$668	\$51,461	\$6,409	\$10,558	\$242
Debt issuers not incl. in Fiscal Plan								
PREPA	8,259	—	—	697	8,956	36	2,775	6
PRASA ⁷	3,943	28	13	584	4,568	229	995	93
Children's Trust	847	613	—	—	1,460	—	140	85
HFA	542	—	—	—	542	85	134	33
PRICO	—	—	—	98	98	—	—	—
Municipality Related Debt ⁸	556	—	—	1,140	1,696	2,036	n.a.	59
Total	\$14,147	\$641	\$13	\$2,520	\$17,320	\$2,386	\$4,044	\$276
Total	\$55,203	\$7,933	\$2,457	\$3,188	\$68,781	\$8,795	\$14,602	\$518
<i>Less: GDB Bonds (excl. TDF)</i>					(3,766)			
<i>Plus: Loans from GDBMFA Entities</i>					8,795			
Public Sector Debt					\$73,810			

Notes:

- 1) Unpaid principal and interest includes debt service that has been paid by insurers and is owed by the government
- 2) HTA includes Teodoro Moscoso bonds
- 3) GDB private loans includes Tourism Development Fund ("TDF") guarantees
- 4) Includes GDB Senior Guaranteed Notes Series 2013-B1 ("CFSE")
- 5) PRIFA includes PRIFA Rum bonds, PRIFA Petroleum Products Excise Tax BANs, PRIFA Port Authority bonds and \$34.9m of PRIFA ASSMCA bonds
- 6) UPR includes \$64.2m of AFICA Desarrollos Universitarios University Plaza Project bonds
- 7) PRASA bonds includes Revenue Bonds, Rural Development Bonds, Guaranteed 2008 Ref Bonds
- 8) Municipality Related Debt includes AFICA Guyanabo Municipal Government Center and Guaynabo Warehouse for Emergencies bonds

IV. How Has Title III of PROMESA Worked So Far?

C. The impact of Hurricane Maria on the process:

1. While it is too early to know the extent of the impact of Hurricane Maria on the economic problems of Puerto Rico, certain observations can be made:
 - (a) Prior to the hurricane, Puerto Rico owed \$74 billion in debt and over \$50 billion in unfunded pensions.
 - (b) The Control Board has stated that the hurricane may have caused as much as \$95 billion in damages.
 - (c) The Oversight Board has withdrawn a demand for employee furloughs and has given the Governor approval to allocate \$1 billion of Puerto Rico's \$9.6 billion budget to emergency relief efforts.
 - (d) The Oversight Board is reevaluating the Fiscal Plan.

IV. How Has Title III of PROMESA Worked So Far?

- (e) The Oversight Board has requested disaster aid from the United States Congress and the White House. An aid package in the range of \$29 billion is said to be ready for the consideration of Congress.
- (f) The precise form the aid package will take and the method of administering it is unclear. Given the provision of Section 204(d) of PROMESA (“...the Oversight Board shall not exercise applicable authority to impede territorial actions taken to (2) implement a federally authorized or federally delegated program...”), the Oversight Board may not control the disaster aid funds.
- (g) Assumedly, Congress will attempt to shield the new money from claims of creditors.

IV. How Has Title III of PROMESA Worked So Far?

- (h) The Oversight Board, HTA and PREPA filed a motion in the Title III case to protect any federal disaster relief funds from the claims of existing creditors or third parties. The court granted the motion on October 25, 2017. The federal disaster relief funds will be used solely for their intended purposes and will be deposited into a segregated and non-commingled account. To the extent the Commonwealth asserts a reimbursement claim against a non-federal entity (instrumentalities, public corporations, municipalities, and other non-federal entities, including PREPA and HTA) for such disaster relief funds the reimbursement claim shall be a super-priority, administrative expense claim in such non-federal entity's Title III case.

IV. How Has Title III of PROMESA Worked So Far?

2. There will be no federal bailout of the existing public debt:
 - (a) President Trump's comment that \$73 billion in debt may be forgiven or wiped out has been clarified by U.S. Budget Director Mulvaney. Debtholders should not expect a federal bailout of the public debt, and the PROMESA Title III process will have to go forward with respect to this debt. What assets will be available to satisfy the creditors remains to be seen.

IV. How Has Title III of PROMESA Worked So Far?

3. A long-range economic recovery plan with a Marshall-type plan for reinvesting and resurrecting essential government services and infrastructure at the desire level to facilitate the economic growth and recovery of Puerto Rico:

As noted above, the Marshall-type plan for Puerto Rico will provide needed infrastructure improvements stimulants and services necessary to economic development and financial recovery. The focus would be establishing Puerto Rico as the center of commerce for the Caribbean in banking, finance, shipping, and foreign trade zone manufacture, assembly and processing. Puerto Rico could be enhanced with new expanded banking and financing powers like the Cayman Islands for specialized investments.

IV. How Has Title III of PROMESA Worked So Far?

D. Significant issues to be resolved in the Title III proceeding:

1. Whether the Title III petition should be dismissed because its filing was not authorized by a validly constituted oversight board:
 - (a) Several hedge funds (Aurelius, *et al.*) have moved to dismiss the Title III petition on the grounds that the Oversight Board members are principal officers of the United States and were required to be appointed with the advice and consent of the Senate.

IV. How Has Title III of PROMESA Worked So Far?

(b) In addition, these funds have moved for relief from the automatic stay to pursue an independent action for declaratory and injunctive relief outside the Title III case against the Oversight Board and its members on the grounds that they were appointed in violation of the Appointments clause of the United States Constitution (as officers of the United States with the advise and consent of the Senate – Senate confirmation) and that the Oversight Board violates the separation of powers.

2. The dispute between general obligation and COFINA bondholders:

(a) COFINA and General Obligation Bonds. One of the major issues in the Title III case is the dispute between the \$12.7 billion of general obligation bonds and the \$17.3 billion of COFINA bonds.

IV. How Has Title III of PROMESA Worked So Far?

- (b) General obligation bondholders claim to "available revenues." The general obligation bonds are, pursuant to the island's constitution, payable from "all available revenues." (P.R. Const. Art. VI § 8) There is no pledge of specific tax revenues but a pledge of "full faith and credit." Constitutional mandate of payments has been recognized by some courts as effective provided consistent with the constitutional language. *Flushing Nat'l Bk. V. Mun. Assistance Corp.*, 40 NY at 731 (1976).

IV. How Has Title III of PROMESA Worked So Far?

- (c) COFINA bondholders claim pledged sale tax revenues not available to others and dedicated with statutory lien to pay COFINA bonds. The COFINA bonds are backed by a special, dedicated sales tax that is subject to a lockbox arrangement in favor of the COFINA bonds. They do not constitute debt of the Commonwealth of Puerto Rico. There is a specific Puerto Rico statute that declares the COFINA bonds have a statutory lien on the sale tax collected. (See Act 18 of 2009 as amendment to Act 91.) Also, there is a claim that the pledge of sale tax revenues for payment of the COFINA bonds also has special revenue protection.

IV. How Has Title III of PROMESA Worked So Far?

- (d) The COFINA/general obligation bondholders dispute. The general obligation bondholders assert that "all available revenues" includes the sales tax pledged to pay COFINA bonds. The COFINA bondholders, who pursuant to the bond resolution claim an interest in the sales tax revenues, dispute this assertion, and claim the sales tax is dedicated to their payments based on special revenues and statutory lien argument and is not available to general obligation holders. Further, if the general obligation bonds can claim "available revenues," would there be anything left for other creditors or to fund necessary costs of essential services?

IV. How Has Title III of PROMESA Worked So Far?

- (e) COFINA bondholders have rights. From the perspective of the COFINA bondholders, the COFINA bond proceeds were used to pay the Commonwealth of Puerto Rico for sales tax revenues to be pledged, collected and used to pay the COFINA bondholders. Such sales tax revenues "purchased" by the proceeds of the COFINA bonds are not from the perspective of COFINA bondholders "available revenues" to pay general obligation debt. Statutory liens and special revenues pledges are to be respected in Chapter 9 and Title III. The COFINA bond trustee has filed an interpleader action (Adv. Proc. No. 17-00133) for a determination of these rights.

IV. How Has Title III of PROMESA Worked So Far?

- (f) General obligation bondholders have rights. On the other hand from the perspective of the general obligation bondholders, they read the mandate of Article VI § 8 of the Puerto Rico constitution "available revenues" as including sales tax revenues pledged to pay COFINA bonds as available to pay general obligation bonds. Further, certain general obligation bondholders assert that "claw back" revenues required to pay constitutional debt and certain property taxes are special revenues with the benefit of a statutory lien (Adv. Proc. No. 17-03283).
- (g) The real issue. If Puerto Rico does not recover and melts financially, how do general obligation bondholders and COFINA bondholders get paid given all their respective rights?

IV. How Has Title III of PROMESA Worked So Far?

- (h) Levels of COFINA debt. In addition, there are two levels of the \$17.3 billion of COFINA bonds:
- The Senior COFINA bonds are owed \$7.6 billion and the Junior COFINA bonds are owed \$9.7 billion.
 - Thus far, the Oversight Board has not taken a position on the merits of the general obligation-COFINA dispute but has stated Puerto Rico cannot satisfy all these debt obligations.
 - Section 510(a) of the Bankruptcy Code, which is incorporated into Title III of PROMESA, specifically recognizes that subordination agreements are enforceable in Title III to the same extent such agreements are enforceable under applicable non-bankruptcy law.

IV. How Has Title III of PROMESA Worked So Far?

- (i) Commonwealth-COFINA – independent agents – dispute resolution mechanisms. The Oversight Board requested court approval of procedures to govern the Commonwealth-COFINA dispute, including the appointment by the Oversight Board of "independent agents" to represent the two parties to litigate or settle the dispute. The court has approved a stipulation providing a procedure to resolve the Commonwealth-COFINA dispute. The Creditors' Committee will serve as the Commonwealth Agent. Bettina Whyte, who has retained separate counsel for this engagement, will serve as the COFINA Agent. A litigation schedule has been proposed to enable the court to rule on the dispute before December 15, 2017. If there is a proposed settlement and the representative of the Ad Hoc Group of G.O. Bondholders and Assured Guaranty Corp. object to the settlement, the settlement shall not be filed with the court unless approved for presentation by Judge Houser, the Mediation Team Leader. A revised Joint Stipulation and Scheduling Order for the Commonwealth-COFINA dispute, which provides for motions for summary judgment on or before November 6, 2017 and a hearing on the dispute December 4-8, 2017, has been filed with the Court. Given the devastation of Hurricane Maria, this hearing may be delayed given the need to address the governmental services needs of the Puerto Rican citizens.

IV. How Has Title III of PROMESA Worked So Far?

3. Other problems the Commonwealth must address in order to recover financially:
 - (a) In the Oversight Board's statement in connection with the Title III Petition of the Commonwealth of Puerto Rico, the Oversight Board referred to the other problems facing Puerto Rico that led to that filing, including:
 - massive pension liabilities and underfunding,
 - collapse in housing and investment,
 - mounting Medicare program but only fraction covered by federal funds and other alleged inequality in Puerto Rico's treatment,
 - declining population,
 - high poverty rate with many citizens requiring welfare and other benefits and how labor participants rate,

IV. How Has Title III of PROMESA Worked So Far?

- inability to fund basic governmental operations as well as needed infrastructure improvements, and
 - need for economic development and increased business opportunities in Puerto Rico.
- (b) Unions have filed adversary proceedings against the Commonwealth (Adv. Proc. No. 17-00242) and PREPA (Adv. Proc. No. 17-00229) asserting that the Fiscal Plan and the 2017-2018 budgets improperly impair collective bargaining agreements in violation of the U.S. Constitution and cannot be enforced.
- (c) The Oversight Board had filed an adversary proceeding against the Governor for the enforcement of the provisions of the Fiscal Plan providing for furloughs of government workers, the reduction of Christmas bonuses and reduction of pension benefits. This adversary proceeding has been voluntarily dismissed without prejudice.

IV. How Has Title III of PROMESA Worked So Far?

4. Public corporation public debt financings require the projects or systems to continue to operate in order for their creditors to be paid:
 - (a) Special revenue bond financings for certain public corporation. The financings for PREPA, HTA, PRASA and others claim to be special revenues financings which, as noted above, have special unimpaired treatment of the pledged revenues as collected by the project or system to be paid to their bondholders in a Chapter 9 or Title III.

IV. How Has Title III of PROMESA Worked So Far?

- (b) Continual funding of operations of the projects and systems is necessary to be able to pay their respective bondholders. It is a truism that, without funding of operations and maintenance of the financing of certain public corporations in Puerto Rico, the bonds cannot be paid. As noted above, Section 928(b) of the Bankruptcy Code provides for funding necessary operating costs in order to assure the ultimate payment of the associated debt.

IV. How Has Title III of PROMESA Worked So Far?

- (c) Feasible, affordable and sustainable plan for operating the project or system provides the best resolution for its debt holders. Regardless of claims of "gross revenues" pledges that require all revenues to be used to pay bonds before the payment of operations and maintenance costs, the only long-term solution to the financial distress of such entities is a feasible recovery plan that pays the necessary operating and maintenance costs to ensure continual operation so that the revenues, needed to pay the bonds, continue to flow. This symbiotic relationship between the need for the continual operation of the enterprise to generate revenue that is required as the source of payment on the bonds should facilitate constructive and feasible restructuring of debt.

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

ADV Case No.	17-00133
Title III Case	COFINA
Plaintiffs	The Bank of New York Mellon as Trustee for the Senior and Subordinated COFINA Bonds
Defendants	Puerto Rico Sales Tax Financing Corporation ("COFINA"); Whitebox Multi-Strategy Partners, L.P.; Whitebox Asymmetric Partners, L.P.; Whitebox Institutional Partners, L.P.; Pandora Select Partners, L.P.; AMBAC Assurance Corporation; Franklin Advisers, Inc.; and CEDE & Co.
Issues Raised	<ul style="list-style-type: none">• Did the restructuring activities prior to the enactment of the Compliance Law passed to effectuate the Fiscal Plan constitute a default under the Indenture;• What is the effective date of Event of Default for the pre-Title III non-monetary defaults noticed May 4 after the May 3, 2017 filing;

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

Issues Raised (cont'd)	<ul style="list-style-type: none">• Was the Trustee required to comply with pre-Title III direction from bondholders that did not comply with the Indenture; and• Does the Trustee have a right to appoint a separate trustee for the Subordinated Bonds.
Relief Sought	<ul style="list-style-type: none">• Interpleader of debt service payments given competing demands by holders, Senior and Subordinated, and COFINA;• Declaration that prior to Title III filing on May 3, no Event of Default;• Determination of right to appoint a separate trustee for the Subordinated COFINA Bonds;• Declaration no duty to act pursuant to demands of holders that did not offer indemnity; and• Declaration that automatic stay does not apply to funds in Trustee's possession.

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

- Bond insurer notice of default. Prior to the Title III filing on May 3, 2017, the trustee for the COFINA bonds, Bank of New York Mellon, had not declared an event of default under the indenture but AMBAC, the bond insurer had given a notice of default on May 1, 2017.
- Disputed effect of the notice of default. According to the Senior COFINA bondholders, this should trigger the stoppage of payments to the COFINA Subordinated Bonds and prioritization of payments to the Senior COFINA Bonds.
- June 1, 2017 interest payout. Immediately after the Title III filing, an issue arose as to the June 1 interest payment due on the COFINA bonds.

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

- Interpleader action as to funds held by the bond trustee.
The bond trustee filed an interpleader action, suggesting the Commonwealth of Puerto Rico had called into question its commitment to honoring the sales tax pledge to COFINA, and seeking court direction as to what action the bond trustee should take with respect to the June 1 payment of \$16,297,863.78. The bond trustee cited the competing claims of the Senior and Subordinated COFINA Bonds, competing demand regarding acceleration of the bonds, and whether there is a default under the indenture and requesting permission to hold the disputed funds pending the court's determination.

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

- Court order approving interpleader. The court granted the request of the bond trustee and ordered:
 - the bond trustee shall interplead the June 1 payment and any future payments pending the court determination of the right to the disputed funds,
 - staying actions against the bond trustee, and
 - requiring parties claiming a right to the disputed funds appear in the adversary proceeding and assert their rights.
- Scheduling order. At the conclusion of the May 30, 2017 hearing on the interpleader action, the court instructed the parties to file initial submissions addressing the issues of nature, sequence, and timing of discovery and motion practice.

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

- Requested modification of interpleader order. At the August 9, 2017 hearing, the Ad Hoc Coalition of COFINA senior bondholders asked that the prior order be modified to allow the bond trustee to make the June 1st payment and that the order be modified to indicate that funds were being held solely for the benefit of the COFINA bondholders. However, the Judge declined to make any changes to the interpleader order at that time.
- The Board may seek access to COFINA funds given the devastation caused by Hurricane Maria.
- Motions for summary judgment must be filed by November 6, 2017.

V. Points to Consider as to Interpleader Action of the COFINA Bond Trustee (17-00133)

- COFINA debt treatment and confirmation of a plan. As noted above, the COFINA bonds with the claimed special revenues pledge and statutory lien given the incorporation into PROMESA of Sections 922(d) and 928 of Chapter 9 should point the way to the quick resolution of this adversary. This is especially interesting because failure to follow the provision of PROMESA and the incorporated Bankruptcy Code sections may make it impossible to confirm a plan of debt adjustment unless the affected COFINA bondholders, trustee and bond insurer agree.

VI. Points to Consider as to Adversary Complaint Brought by Insurers (17-00125)

ADV Case No.	17-00125
Title III Case	Commonwealth
Plaintiffs	Assured Guaranty Corp.; Assured Guaranty Municipal Corp.; and National Public Finance Guarantee Corporation (insurers of various bonds – G.O. Bonds, PBA Bonds, HTA Bonds, CCDA Bonds, IFA Bonds)
Defendants	Commonwealth of Puerto Rico; The Financial Oversight and Management Board for Puerto Rico; Puerto Rico Fiscal Agency and Financial Advisory Authority; Hon. Ricardo Antonio Rossello Nevares; Gerardo Portela Franco; Hon. Raul Maldonado Gautier; and John Does 1-3

VI. Points to Consider as to Adversary Complaint Brought by Insurers (17-00125)

Issues Raised	<ul style="list-style-type: none">• <u>Compliance with the law.</u> Commonwealth's Fiscal Plan dated March 13, 2017 ("Illegal Fiscal Plan") and Fiscal Plan Act, which implemented the Illegal Fiscal Plan, violate PROMESA, Section 201(b)(1)(N), that requires any Fiscal Plan must respect lawful liens and priorities, Section 201(b)(1)(M), which requires a Fiscal Plan must ensure assets for a territorial instrumentality not transferred except in accordance with the law;• <u>Confiscation of special revenues.</u> Illegal Fiscal Plan violates PROMESA by allowing the Commonwealth to simply misappropriate for its own general use <u>special revenues</u> that constitute the property of its public corporations and their bondholders; and• <u>Impairing contractual rights.</u> This also violates the U.S. Constitution contracts clause, taking clause and due process.
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VI. Points to Consider as to Adversary Complaint Brought by Insurers (17-00125)

Relief Sought	<ul style="list-style-type: none">• Declaratory judgment that: Illegal Fiscal Plan and Fiscal Plan Act violate PROMESA, the Contracts Clause, the Taking and Due Process Clauses of the Constitution;• Order enjoining any action pursuant to Illegal Fiscal Plan and Fiscal Plan Act; and• Order staying confirmation pending the development of Fiscal Plan compliant with PROMESA and U.S. Constitution.
Status	<ul style="list-style-type: none">• Following Hurricane Maria, the insurers voluntarily dismissed this adversary proceeding without prejudice.

VI. Points to Consider as to Adversary Complaint Brought by Insurers (17-00125)

- Violation of laws and constitutional provisions. The insurers had asserted the Fiscal Plan violates the terms of PROMESA (because it fails to respect lawful priorities and liens), and the contracts, takings and due process clauses of the U.S. Constitution.
- Stay of confirmation and protection of special revenues. Among the relief sought was a stay of the confirmation of any plan that is based upon the Fiscal Plan. Section 314 of PROMESA requires that the plan of adjustment and the implementation thereof comply with the provisions of PROMESA and the Bankruptcy Code incorporated therein. As noted above, special revenues, as alleged here by the insurers, are to be unimpaired by the Title III filing and failing to do so may be fatal to confirmation of a plan of debt adjustment if plan does not provide the bonds in question are to be paid by statutory liens, special revenues or an enforceable constitution mandate for payment unless the affected creditors consent.

VI. Points to Consider as to Adversary Complaint Brought by Insurers (17-00125)

- Reversal of Court's denial of Creditor Committee intervention. The Court had denied the request of the Unsecured Creditors Committee to intervene in the proceeding. The Committee has appealed this ruling to the First Circuit, which reversed the ruling but held the precise scope was in the discretion of the District Court. 2017 U.S. App. LEXIS 18387 (1st Cir. Sept. 22, 2017).
- Lack of standing and statutory liens. The Oversight Board had argued in briefing that the insurance companies lack standing, that PROMESA § 106(e) precludes this challenge to the Fiscal Plan, and that they do not have statutory liens.

VII. Points to Consider as to Adversary Complaint Brought by a Holder of the HTA Uninsured Bonds (17-00151)

ADV Case No.	17-00151
Title III Case	Commonwealth; Puerto Rico Highways & Transportation Authority ("HTA")
Plaintiffs	Peaje Investments LLC, holder of \$65 million in uninsured HTA Bonds
Defendants	HTA, Hon. Carlos Contreras Aponte, The Commonwealth of Puerto Rico, Hon. Ricardo Rossello, Hon. Raul Maldonado Gautier, Hon. Jose Ivan Marrero Rosado, Puerto Rico Fiscal Agency and Financial Advisory Authority, Hon. Gerardo Portela Franco
Issues Raised	<ul style="list-style-type: none">• Are Toll Revenues pledged as collateral for HTA Bonds special revenues and subject to a statutory lien?• Does the automatic stay apply to the Toll Revenues?

VII. Points to Consider as to Adversary Complaint Brought by a Holder of the HTA Uninsured Bonds (17-00151)

Issues Raised (cont'd)	<ul style="list-style-type: none">• Is the action by HTA diverting the Toll Revenues and failing to deposit those revenues with the Fiscal Agent unlawful?• Can the special revenues be used for operating expenses for other than expenses necessary to preserve the Toll Roads, the system that generates the Toll Revenues?
Relief Sought	<ul style="list-style-type: none">• Declaratory judgment that Toll Revenues are pledged special revenues, not subject to automatic stay, subject to statutory lien;• Declaratory judgment that expropriation of Toll Revenues violates Fifth Amendment and other laws; and• Determination of the extent to which Toll Revenues can be used for operating expenses.

VII. Points to Consider as to Adversary Complaint Brought by a Holder of the HTA Uninsured Bonds (17-00151)

Status	<ul style="list-style-type: none">• The matter has been referred to the Magistrate for general pre-trial management; and• Following a hearing on the Plaintiff's Motion for a Preliminary Injunction and for Relief from the Automatic Stay or for Adequate Protection, the Bankruptcy Court ruled the plaintiff as a bondholder of the HTA Bonds failed to show that the bonds had a statutory lien on revenues of the HTA and failed to demonstrated there was an erosion of the equity cushion of the value of the secured collateral over the amount of debt owed. Based on the expert testimony provided, the court held the plaintiff failed to demonstrate cause to lift the automatic stay. The plaintiff failed to focus its argument that the HTA bonds have special revenues pledged to pay the bonds and that under Section 922(d) and 928(a) net special revenues after the payment of current costs of operation
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VII. Points to Consider as to Adversary Complaint Brought by a Holder of the HTA Uninsured Bonds (17-00151)

Status (cont'd)	<p>(operation and maintenance costs as defined in the operative documents) are not stayed and must be paid to the bondholders of the HTA Bonds. Expert testimony had focused on the “irrelevant equity cushion” rather than the actual net special revenues available after paying for operation and maintenance costs required to be paid by the terms of the documents and Section 922(d) and 928(a) of the Bankruptcy Code. The court also denied the Unsecured Creditors Committee’s motion to intervene in the actions. Given the Court’s ruling, the plaintiff has filed an amended complaint alleging the special revenue status of the revenues pledged to pay the bonds.</p>
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VII. Points to Consider as to Adversary Complaint Brought by a Holder of the HTA Uninsured Bonds (17-00151)

- Diversion of funds. This beneficial holder of \$65 million of uninsured HTA Bonds challenges as illegal the post-filing diversion of tolls from the HTA and failure to deposit the tolls with the fiscal agent.
- Special revenues and statutory liens issues and confirmation of a plan. The bondholder asserts the tolls are special revenues and subject to a statutory lien. Again, if it can be demonstrated that the HTA Bonds are to be paid by special revenues or a statutory lien, failure to comply with the provisions of PROMESA and the provisions of the Bankruptcy Code incorporated therein could be fatal to being able to having a plan of adjustment confirmed unless the affected creditors consent.

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

ADV Case No.	17-00155
Title III Case	Commonwealth and Puerto Rico Highways & Transportation Authority ("HTA")
Plaintiffs	Assured Guaranty Corp.; Assured Guaranty Municipal Corp.; Financial Guaranty Insurance Company; National Public Financial Guarantee Corporation, insurers of HTA Bonds
Defendants	Commonwealth of Puerto Rico; Financial Oversight and Management Board for Puerto Rico; Puerto Rico Fiscal Agency and Financial Advisory Authority; Puerto Rico Highways and Transportation Authority; Hon. Ricardo Antonio Rossello Nevares; Gerardo Portela Franco; Carlos Contreras Aponte; Jose Ivan Marrero Rosado; Hon. Raul Maldonado Gautier; and Natalie A Jaresko

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

Issues Raised	<ul style="list-style-type: none">• Are the HTA Bonds secured by a gross lien on pledged Toll Revenues of HTA, gasoline, diesel, crude oil and other special excise taxes and motor vehicle license fees collected by the Commonwealth?• Do these constitute special revenues and contractual liens?• Is the Fiscal Plan that diverts the HTA pledged revenues to the General Fund illegal?• Given gross pledge, can pledged revenues be used for all HTA expenses and can special excise taxes be used for this purpose?
Relief Sought	<ul style="list-style-type: none">• Declaratory relief that filing of Title III petition does not operate as a stay of pledged special revenues;

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

Relief Sought (cont'd)	<ul style="list-style-type: none">• Finding that failure to remit special revenues violates Sections 922(d) and 928(a) of the Bankruptcy Code and injunction against such further violations; and• Ordering Defendants to remit revenues securing the HTA Bonds.
Status	<ul style="list-style-type: none">• Motion to Dismiss has been filed and a hearing is scheduled on November 21, 2017;• A Stipulated Order has been entered providing the disputed funds would be maintained in the existing accounts and invested per the governing documents pending further order of court without prejudice to the ability of the parties to make arguments regarding the disputed funds; and• The case has been referred to the Magistrate for pre-trial management.

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

- Claim special revenue status. The bond insurers filed an adversary complaint in the Commonwealth of Puerto Rico and HTA cases with respect to bonds issued by HTA in which they assert the HTA bonds are secured by special revenues and a contractual lien.
- Diversion of funds. The bond insurers allege that, since November 2015, the Commonwealth and HTA diverted the pledged special revenues from payment of the HTA bonds to the Commonwealth's General Fund.
- Fiscal Plan creates the problem. Further, they allege the Fiscal Plan implements and perpetuates the contract impairment and illegal confiscations of property.

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

- Requested special revenues protection. The bond insurers seek enforcement of the special revenue protections of the Bankruptcy Code (11 U.S.C. §§902, 922(d), 928(a)), which Congress incorporated into Title III, a declaration that the payment of special revenues is not subject to the automatic stay, and injunction against a further violation of Sections 922(d) and 928(a). Again, if it can be demonstrated that the HTA Bonds are to be paid by special revenues, failure to follow the provisions of PROMESA and the incorporated therein provisions of the Bankruptcy Code may make it impossible to confirm a plan of debt adjustment unless the affected creditors consent.

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

- Ambac adversary. A separate but similar adversary proceeding was brought by AMBAC seeking:
 - a declaratory judgment that the Fiscal Plan and Fiscal Plan Compliance Act are unconstitutional and illegal;
 - an injunction against presenting, continuing, modifying or confirming any plan of adjustment promised on the illegal Fiscal Plan or Fiscal Plan Compliance Act;
 - An injunction against taking any other actions based upon, or pursuant to, the Fiscal Plan or Fiscal Plan Compliance Act, including any action relating to future legislation, rules, or budgets;

VIII. Points to Be Considered in Connection with Adversary Complaint Brought by Certain Bond Insurers of HTA (17-00155)

- a declaratory judgment that the HTA Pledged Special Revenues are pledged special revenues under the Bankruptcy Code (as incorporated by PROMESA);
- A declaration that Defendants' post-petition actions have violated the pledged special revenue protections established by the Bankruptcy Code;
- An injunction preventing Defendants from taking any action that would impair, or continue the impairment of the free flow of HTA Pledged Special Revenues to HTA and the HTA Revenue Bondholders; and
- A hearing on the Motion to Dismiss this complaint is scheduled for November 21, 2017.

IX. Points to Consider as to Adversary Complaint Brought by the Representative Organization of Professors at University of Puerto Rico (17-00197)

ADV Case No.	17-00197
Title III Case	All Article III Debtors except PREPA
Plaintiffs	Asociacion de Profesoras y Profesores Del Recinto Universitario De Mayaguez, inc. (APRUM)
Defendants	Commonwealth of Puerto Rico; the Financial Oversight and Management Board for Puerto Rico; Hon. Ricardo Antonio Rossello Nevares; Gerardo Portela Franco; Hon. Raul Maldonado Gautier; Jose Ivan Marrero Rosado; Natalie A Jaresko and John Does 1-5
Issues Raised	<ul style="list-style-type: none">• Does the Fiscal Plan, that cuts \$201 million for the University of Puerto Rico's 2017-2018 budget, violate PROMESA by failing to provide sufficient resources for an essential service?

IX. Points to Consider as to Adversary Complaint Brought by the Representative Organization of Professors at University of Puerto Rico (17-00197)

Relief Sought	<ul style="list-style-type: none">• Declaratory Judgment that:<ul style="list-style-type: none">• UPR's services are essential public services;• The Fiscal Plan violates PROMESA because it neglects funding this essential service;• The Oversight Board's determination as summarized in the Fiscal Plan and imposed in the 2017-2018 budget are arbitrary, lacking in national bases and in violation of the Due Process of Law; and• The 2017-2018 budget should be totally recast to ensure the funding of essential public services.• An injunction from presenting any plan of adjustment until the Fiscal Plan is recast to comply with the law and the U.S. Constitution.
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IX. Points to Consider as to Adversary Complaint Brought by the Representative Organization of Professors at University of Puerto Rico (17-00197)

Status	<ul style="list-style-type: none">• Motion to Dismiss filed. An amended complaint will be filed, and any Motion to Dismiss the amended complaint will be heard March 7, 2018; and• Matter referred to Magistrate for pre-trial management.
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X. Points to Consider as to Adversary Complaint Brought by Holders of Bonds Issued by the Employees Retirement System (ERS) of the Government of the Commonwealth of Puerto Rico (17-00189)

ADV Case No.	17-00189
Title III Case	Commonwealth; The Employees Retirement System of the Government of Puerto Rico ("ERS")
Plaintiffs	Numerous funds holding the ERS Bonds
Defendants	The Commonwealth of Puerto Rico; the Financial Oversight and Management Board of the Commonwealth of Puerto Rico; the Puerto Rico Fiscal Agency and Financial Advisory Authority; the Employees Retirement System of the Government of Puerto Rico; Governor Ricardo Antonio Rossello Nevares; Hon. Raul Maldonado Gautier

X. Points to Consider as to Adversary Complaint Brought by Holders of Bonds Issued by the Employees Retirement System (ERS) of the Government of the Commonwealth of Puerto Rico (17-00189)

Issues Raised	<ul style="list-style-type: none">• Do the ERS bond owners have a claim secured by all employer contributions from Puerto Rico Government employers and was Joint Resolution 188 adopted by the Oversight Board, that requires ERS to liquidate its assets for distribution to the Commonwealth General Fund and directs employers to make future contributions to the General Fund enforceable?
Relief Sought	<ul style="list-style-type: none">• A declaration that Joint Resolution 188 cannot be implemented;• A determination of the secured status of the ERS bonds;• A declaratory judgment that any transfer to pledged property pursuant to Joint Resolution 188 will result in unjust enrichment; and

X. Points to Consider as to Adversary Complaint Brought by Holders of Bonds Issued by the Employees Retirement System (ERS) of the Government of the Commonwealth of Puerto Rico (17-00189)

Relief Sought (cont'd)	<ul style="list-style-type: none">• A declaratory judgment that transfer of Plaintiffs' collateral was not for a public use and violates the U.S. and P.R. Takings and Contracts Clauses.
Status	<ul style="list-style-type: none">• A hearing on the Motion to Dismiss the complaint is scheduled for November 30, 2017.

XI. How the Best Recovery for Puerto Rico and for Its Creditors Are One in the Same

- A. There is no substitute for the practical ability to be paid from a plan of adjustment and fiscal plan that maximize value and recoveries to the extent reasonable and reinvest in Puerto Rico to ensure continual operations and sufficient tax revenues to reasonably pay off its creditors:
1. If there is no money, there is no payment no matter the rights or priorities. All the rights legally possible do not necessarily translate into payment of public debt. Governments cannot pay money they do not and will not have.

XI. How the Best Recovery for Puerto Rico and for Its Creditors Are One in the Same

2. Now is the time for all parties to unite, resolve differences and develop a recovery plan and support economic development strategies and Marshall-type plan to rebuild the Puerto Rico's infrastructure. Now is the time for creditors in Puerto Rico to unite and develop a constructive plan of adjustment based on a fiscal plan acceptable to Puerto Rico, the Oversight Board and major creditor groups. The failure to obtain those parties' agreement can be fatal to all. Also, there should be a recognition that reinvesting in Puerto Rico, its services and infrastructure, as well as economic development, is part of any feasible plan in the best interest of creditors. The development of the economic recovery plan and a Marshall-type plan to reshore and enhance essential services and needed infrastructure to a level required for economic development and to attract new businesses to Puerto Rico or encourage businesses in Puerto Rico to expand in Puerto Rico creating new, good jobs that produce additional new taxpayers that results in new tax revenues that funds financial recovery, essential services, needed infrastructure improvement and the ability to pay creditors.

XI. How the Best Recovery for Puerto Rico and for Its Creditors Are One in the Same

3. Provide an effective method of addressing those short-term creditors who do not want to be part of the recovery process. Public debt holders who are short-term holders, who do not want a longer term commitment to work out this distress situation could be offered a tender or exchange offer, a payment at a determined discount that will allow their exit at a price no more than the projected value of the recovery to their class of creditors. Financing of such tender or exchange offer could be approved by the Oversight Board with "good as gold" protections under § 364(c) or 364(d) of the Bankruptcy Code permitted under Section 304(e) of PROMESA with priority and security for access and low borrowing cost that would further increase the benefit of the tender or exchange offer.

XI. How the Best Recovery for Puerto Rico and for Its Creditors Are One in the Same

4. Maximize value and recovery through financial alchemy. Creative and constructive engagement of creditors in long-term investment and profits of economic development of Puerto Rico could reduce the cash cost of satisfying debt obligations with development rights, operational rights or upside rights related to the Puerto Rico enhanced and improved operations. This could be through new business opportunities, restructuring existing operations or public-private partnerships.
5. Use creative legislative and administrative actions by the Federal Government and Puerto Rico. Consideration of special economic zones for Puerto Rico, equal treatment by federal policies and programs, special tax incentives or tax credits for economic and business development in Puerto Rico could be used to help "prime the economic pump."

XI. How the Best Recovery for Puerto Rico and for Its Creditors Are One in the Same

B. A litigated resolution is not the best result for Puerto Rico or its creditors:

1. A litigated Title III plan of adjustment with accompanying appeals possibly to the U.S. Supreme Court could cost Puerto Rico and its creditors hundreds of millions that could have been reinvested in Puerto Rico or paid to creditors.
2. Time delay of litigation destroys the ability to obtain the best result.
3. The stigma of litigation destroys the ability to move forward quickly and effectively with economic recovery. See *e.g.*, Greece, Ecuador, Argentina, Brazil, *et al.*

XI. How the Best Recovery for Puerto Rico and for Its Creditors Are One in the Same

- C. The prompt development of a feasible, sustainable and affordable plan of adjustment agreed to by the Oversight Board, Puerto Rico and major creditors is the best scenario for all.

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