ABSTRACT

In January 2022, a federal judge ruled that a new debt restructuring framework for Puerto Rico would be in effect to partially relieve the island of its debt obligations to creditors. Despite the judge’s ruling, Puerto Rico remains in a vulnerable economic state and a dysfunctional political environment with a slight projection for growth. Without growth, debt sustainability is a challenge. This proposal to the Majority Leader Chuck Schumer offers adjustments to the excising PROMESA law, which focuses on debt restructuring and fiscal oversight.

The recommendation creates a more equitable Medicaid system and expands Medicaid funding for Puerto Rico beyond the statutory limits, along with implementing a Medicaid-focused control mechanism to minimize fraud, waste, and abuse. By stabilizing Medicaid, one of the main cost drivers in Puerto Rico, debt sustainability is a strong possibility, and the territory will be able to meet financial obligations to creditors and its citizens. This paper further examines the current political climate within the Democratic-held Congress and the Executive branch.

Advised by: Professor Paul Weinstein
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TO: Majority Leader Charles Schumer (D-NY)
FROM: Magdalene Bramlett
DATE: May 5, 2022
SUBJECT: Proposal to stabilize Puerto Rico’s debt through Medicaid equity

I. ACTION FORCING EVENT

On January 18, 2022, Federal Judge Laura Taylor Swain approved a debt restructuring plan reducing remaining obligations to help Puerto Rico recover from its debt and the associated austerity measures\(^1\). The new debt restructuring plan is the latest step toward Puerto Rico’s financial recovery after the fiscal control board failed to deliver under the Puerto Rico Oversight, Management, and Economic Stability Act, known as PROMESA. On June 30, 2016, former President Barack Obama signed PROMESA to relieve the struggling US territory from a pending economic crisis following its governor’s announcement that the island’s debt burden is unsustainable.\(^2\)

II. STATEMENT OF THE PROBLEM

Although the newly approved debt restructuring plan reduces Puerto Rico’s debt claims by approximately 34 billion dollars to 7 billion dollars\(^3\), thus lowering the Commonwealth’s debt payments significantly, the island must ensure that its persisting debt is sustainable. Despite being a US territory, the island continues to lack fiscal stability. Data indicate that Puerto Rico’s infrastructure, a strong indicator of economic activity, remains in disarray with 43.5% of Puerto

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Ricans living in poverty. The primary issue is Puerto Rico’s ambiguous political identity as a US Commonwealth, inevitably affecting its economic status and relationship with the United States. Under the circumstances of political uncertainty, it is challenging for Puerto Rico to establish a functioning and stable economy independent of restrictions and regulations placed on them many decades ago.

Growth is necessary to meet the remaining obligations and simultaneously provide enough resources to support social programs that are in place to prevent the poverty rate from rising. Also, growth calls for expansionary policies, which require an influx of capital into Puerto Rico’s economy. The island cannot take on new debt to finance expansionary policies, and new financial institutions are apprehensive toward the prospect of providing capital for Puerto Rico, given the financial uncertainty. In fact, Puerto Rico’s, “annual economic growth fell by roughly 12.5% overall between 2004 and 2020” and the island’s population numbers declined by more than 16%.

In a policy brief, de Rugy and Salmon point out that “the empirical evidence overwhelmingly supports the view that a large amount of government debt has a negative impact on economic growth potential, and in many cases that impact gets more pronounced as

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9 Ibid 8
debt increases.” After examining existing literature that studied debt-growth ratios and their effects, the researchers conclude that there is an inverse relationship between debt burden and potential growth. Applying their findings on the situation in Puerto Rico, the island’s presumption that it could grow economically while indebted was never achieved.

A recent debt sustainability analysis11 discusses Puerto Rico’s economic situation and provides insights based on currently approved and predicted fiscal plans and growth rates for the years leading up to 2027. According to the projections, Puerto Rico’s debt is unsustainable in the long run as it would require surpluses in the range of 3.5% to 7.4% of GNP in the immediate future and in perpetuity. The economists Gluzmann, Guzman, and Stiglitz12 proposed different debt restructuring scenarios and concluded that Puerto Rico could recover when these projected growth rates are met.

Because of Puerto Rico’s fragile economic condition, unique status as a US territory, and geographic location affected by the consequences of unpredictable natural disasters, growth plans are volatile, complicating the island’s ability to forecast accurately. Another forecast shows an annual decline in the GDP with an average rate of -0.3%13, suggesting that Puerto Rico’s economy is estimated to shrink rather than grow.

Moreover, the new debt restructuring plan did not fully relieve Puerto Rico from its debt, keeping the debt obligations as an obstacle to allocating funds toward necessary programs and initiatives and addressing other severe issues such as the high poverty rates and the overwhelmed healthcare system. Also, the study was conducted in 2018, before Hurricanes Irma and Maria devasted the island, and thus, the assumption continues to exist that Puerto Rico’s

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12 Ibid 11
economic position worsened. Although Puerto Rico received 140 million dollars in relief payments, which FEMA directed for recovery measures,\textsuperscript{14} the rebuilding process was hampered by the bureaucracy of the procedures associated with Section 428 of the Stafford Act. \textsuperscript{15} Under Section 428 FEMA has full control of the projects and is authorized to take an “alternative procedure” approach to build a resilient infrastructure.

In addition, the COVID pandemic hurt the global economy, and Puerto Rico and its citizens were not immune to the economic devastation caused by the pandemic. Even though the US Federal Government (USFG) distributed recovery funds and stimulus, the islanders could not benefit to the same extent as other US citizens. For example, residents of Puerto Rico were not eligible for advanced child tax credits, significant payments that assisted families to withstand financial downturns.\textsuperscript{16} The crucial benefits are available now, but many families are not informed on the processes involved in filing federal income tax to gain access to these payments, primarily because native Puerto Ricans are exempt from the US federal income tax process.

Puerto Rico’s current issues go beyond the USFG’s initiatives to help the struggling island. The problems are perpetual and rooted in a complex series of intertwined and unstable conditions, such as the inability to repay obligations associated with debt, the prevalent poverty issue, and the poor infrastructure that threatens every aspect of the tiny island’s existence. In a multi-layered crisis, growth is at stake, and Puerto Rico and its people remain vulnerable. To


complicate matters further, Puerto Rico is hindered by the strict regulations imposed by the USFG in the form of the Jones Act from 1920.\(^\text{17}\)

The Jones Act establishes that Puerto Rico’s imports must be transported on a US vessel. So, for example, a ship coming from Asia could not make a stop in Puerto Rico to deliver goods but must go to a US State and circumnavigate the island. The goods can then be brought to the territory by a relatively expensive US vessel. According to a study \(^\text{18}\), this logistic process increases Puerto Rico’s annual cost of transportation by 568.9 million dollars and the prices of goods by 1.1 billion. The imposed Jones Act also deprives the island of jobs in industries related to imports, such as shipbuilding or activities associated with the merchant marine industry, such as the transportation of goods, raw materials, and people. Additionally, due to higher prices, the Act impacts other sectors that cannot create employment opportunities, and the loss in tax revenues is another negative aspect of the Jones Act.

A second analysis\(^\text{19}\) found that Puerto Rico’s food and beverage sector spent 367 million dollars more on products in one year. Considering that one of Puerto Rico’s primary industries is tourism, the island potentially operates on lower price margins to stay competitive in the Caribbean. Consequently, the impoverished citizens spend a higher percentage of their income on imported products, preventing them from rising out of poverty and distributing their capital in a way that would benefit the nation. The Jones Act negatively impacts almost every industry on the island, such as hospitality and the need of basic goods and services, and there currently is no clear path toward amending or abolishing the decades old Act.


Puerto Rico’s political status also hinders the island from gaining access to federal funds in the healthcare sector. As a territory, Puerto Rico is treated differently and is not eligible to receive the same infusions of federal funds for crucial safety net programs, such as Medicare and Medicaid. For Medicaid, the Federal Medical Assistance Percentage (FMAP) is at 55%, slightly above the lowest share (50%) the USFG must provide by law, and the amount is capped to an approx. $400 million. So, despite Puerto Rico’s relatively high reliance on Medicaid, the Commonwealth can only receive assistance up to the amount of the block grant.

That being the case, with high poverty levels and limited access to federal dollars, Puerto Rico spends a higher portion of its finances on Medicaid. The beneficiaries possibly lose quality service when operating under low-cost measures. Consequently, the underfunded health safety nets have a negative effect on economic activity across the island. In a policy brief conducted by the Kaiser Foundation, experts discuss the positive impact Medicaid spending has within the US and in its territories. It creates direct and indirect benefits for various stakeholders, including the municipalities, citizens, service providers, and vendors, in the form of state revenue, income, or employment. On the contrary, reduced spending hurts the economy.

III. HISTORY/BACKGROUND

Puerto Rico’s debt crisis is not attributed to one incident, but it is a sequence of events that were a result of several factors contributing to the dysfunctional economic condition of the island. Before Puerto Rico’s financial predicament, the USFG authorized favorable tax codes to incentivize private corporations to seek out the island as an investment and manufacturing hub.

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Tax breaks were the government’s attempt to jump-start Puerto Rico’s economy. Corporations were encouraged to manufacture in Puerto Rico, which created steady jobs and acted as a driver of growth.

However, the Treasury argued excessive losses to tax revenues, and analysis showed that the primary beneficiaries of the tax incentives were the corporations. Although the island’s economy grew since the implementation of the corporate tax code section 936, the annual average growth rate was not equal to the US States. The initiative underperformed and did not produce the necessary progress and competitiveness to lift Puerto Rico’s economy and its citizens substantially. Therefore, former President Bill Clinton signed a law that phased out section 936 in 2006 after ten preceding years. Puerto Rico lost its attractiveness, and organizations that operated on the island and benefited from the tax loopholes moved to more strategically and financially convenient places.

The end to corporate tax exemptions struck the Commonwealth negatively as Puerto Rico’s government depended on sectors, such as the pharmaceutical industry, to propel development and growth. The exit of businesses created revenue losses and employment declines for the US territory. A study published in the Journal of the Center for Puerto Rican studies estimated that Puerto Rico experienced a “loss of 75 percent of manufacturing jobs relative to service sector industries” due to the elimination of section 936. The government’s attempt to restore economic growth and improve living standards through the manufacturing

25 Ibid 19
sector was interrupted. Puerto Rico’s employment fell by 45% \(^\text{27}\), particularly in manufacturing. Its poverty levels ranging from 40-45 percent exceeded the US national rate of around 13 percent \(^\text{28}\). Population loss and outmigration deepened the vicious cycle.\(^\text{29}\) Puerto Rico’s population shrunk annually since 2006 and was estimated to continue to decrease. With a declining labor force and lower tax revenues that result from reduced population numbers, economic progress remained stalled.

Moreover, Puerto Rico’s officials made ambitious revenue estimates, but the fiscal outlooks deteriorated, and the US territory’s economic situation was on an unsustainable path. \(\text{Figure 1.}\) \(^\text{30}\) displays the increase of deficits between the years 2002 and 2014. In a line-to-line comparison, the graph shows that Puerto Rico’s expenses grew on a larger scale than revenues, increasing the gap substantially. When examining the trendlines in the chart, one can observe a considerable revenue drop in 2008, which appears to be the beginning of the divergence in that era. The following year, in 2009, the graph shows a notable peak in expenses. This increase is a sign of the aftermath caused by the financial crisis in 2008.

\(^{27}\) Ibid 20 page 6
To fund operation expenditures and withstand economic downturns, the Puerto Rican government issued bonds and turned to financial markets on Wall Street. Without regulation mechanisms, borrowing was relatively easy but came at the expense of paying predatory interest rates.\(^{31}\) Falling behind on obligations, the Puerto Rican government also tapped into the pension system for public employees and depleted the system of its assets, and thus, putting Puerto Rican benefit payments at risk. Public pension liabilities were unfunded, and the resulted pension debt rose to $55 billion.\(^{32}\) During the same period, the financial collapse of 2008 added to the dire situation. Consequently, the island further defaulted on payments and lost its creditworthiness.


The United States Government Accountability Office ³³ (GAO) identified three major stressors such as “(1) inadequate financial management and oversight practices, (2) policy decisions, and (3) prolonged economic contraction.” The combination of a lack of proper control and budgetary practices and unmet economic trends created the perfect financial storm. Due to its territory status, Puerto Rico could not declare bankruptcy, unlike Detroit, for instance, a city that defaulted on debt obligations but was able to gain protection from creditors and reassess and reorganize its municipal debt following insolvency approval. ³⁴ Nor could the Commonwealth reach out to the IMF for financial support, which Greece, as a sovereign nation, was able to do when facing a fiscal crisis.³⁵

Nevertheless, to assist Puerto Rico with its fiscal dilemma, in 2016, the Obama Administration enacted PROMESA. Under PROMESA, a Financial Oversight and Management Board (FOMB) advised on a process that aimed to restructure the accumulated debt of over $ 72 billion.³⁶ The initial PROMESA charter from the Obama Administration included additional funding for programs to support Puerto Ricans during the economic crises, such as higher provisions for the healthcare sector; however, the Republican-held Congress did not approve all aspects of the original PROMESA and agreed on a “leaner” version that mainly focused on fiscal oversight and debt restructuring.³⁷

³³ Ibid 30 page 16
³⁴ Ibid 8
³⁶ Ibid 32
One of the primary responsibilities of FOMB was to develop fiscal plans for Puerto Rico’s recovery and further re-establish the island’s access to capital markets. FOMB’s revenue estimates were to be used by Puerto Rico’s Governor to develop budgets which were subject to the board’s approval. The board was ordered to consult Puerto Rico in territorial reforms that would lead to fiscal stability and development. The Governor’s financial operations and aspects of the island’s administrative responsibilities remained under tight control, and Puerto Rico lost its voice and ability to govern itself if it did not fully comply with FOMB’s agenda.

Although PROMESA gave Puerto Rico a quasi-bankruptcy option and debt restructuring powers that it did not have prior to being under FOMB’s microscope, FOMB made decisions that came with strict austerity measures that impacted the Commonwealth’s citizens, who already were struggling. The Center of Popular Democracy reported that “the Board has used its power to impose devastating austerity measures and negotiate unsustainable debt restructuring plans that enrich Wall Street and hurt Puerto Ricans.” PROMESA neglected to implement policies that would help citizens by providing additional funding for social programs. On the contrary, PROMESA denied the Puerto Rican Governor from implementing his proposed economic strategy to move the island forward.

Growth decline persisted as a challenge in an economy with a citizenry that suffers. FOMB’s projections missed some of the island’s vulnerabilities, and thus, the current form of PROMESA has not delivered.

40 Ibid 31
42 Ibid 39
It should be noted that with PROMESA in place, diverse bills were presented to strengthen Puerto Rico, establish its economic stability, and relieve the island from unequal treatment and the drawbacks and disadvantages of its territory status. In 2019, Senator Mike Lee (R-Utah) submitted the “Open America’s Water Act”\(^{43}\), a bill that would eliminate the Jones Act that costs Puerto Rico billions of dollars each year. Although the Jones Act was waived in times of emergency to ease aid distribution\(^{44}\), no permanent repeal has passed Congress. The Congressman Tom McClintock (R-California) also opposes the Jones Act and is supporting Lee’s bill in the Senate\(^{45}\), yet passing of the legislation to repeal the Act faces a steep climb.

In 2021, the bipartisan “Puerto Rico Statehood Admission Act”\(^{46}\) was introduced in Congress, advocating for Puerto Rico to become a US State with full representation, rights, and federal assistance. Also, the US Senate initiated a bill seeking the Commonwealth to become an equal US member. As of now, these bills have not passed and lack the necessary votes in Congress to get out of the early stages of the congressional committee.

The latest approach to relieve the struggling Commonwealth was proposed in 2021 by the Biden Administration in the Build Back Better (BBB) Bill\(^{47}\). The bill included various steps that would serve Puerto Rico. A crucial element is the expansion of social programs such as the Supplemental Security Income benefits, Medicaid, Refundable Tax Credits, and Educational

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Improvement Tax Credits. Increased funding would relieve Puerto Rico from budgetary pressure, allow the territory to assist residents, and establish a more stable economic foundation.

Further, the BBB initiative aimed to invest in Puerto Rico’s goal to address issues associated with climate change\textsuperscript{48}, essential areas required to transform toward a sustainable economy and prepare for future challenges brought on by natural disasters. Despite approval in the House, the BBB framework was never finalized in the Senate. At this juncture, there is no clear indication which policies, if any, will be implemented to assist Puerto Rico.

IV. POLICY PROPOSAL

To support Puerto Rico’s government in the repayment of its remaining debt to its creditors of approximately $7.4 billion\textsuperscript{49}, requiring the territory to allocate roughly $1.15 billion of its general fund budget, I propose an amendment to the existing PROMESA law as a sustainable response that will give the island supplemental tools and resources to meet their financial obligations in the short and long-term. The three components of the response are a request for 1) a permanent increase in federal funding in the form of FMAP, 2) a waiver of the existing cap on the allotment for Medicaid and CHIP, and 3) the establishment of a task force, the PROMESA Medicaid Consultant Unit (PMCU), to safeguard the management of the funding process and appropriate funds earmarked for specific agencies/stakeholders on the island.

The first and second components of the proposal mirror the conditions written into New York Representative Nydia Velázquez’s congressional bill, H.R. 3371\textsuperscript{50}, the Puerto Rico Health Care Fairness, Accountability, and Beneficiary Access Act of 2019. The bill called for a change in “the FMAP percentage from 55% to 83% through FY2029” and further enhancement based on

\textsuperscript{49} Ibid 8
\textsuperscript{50} US HR3371. \textit{BillTrack50}. Accessed March 28, 2022: https://www.billtrack50.com/billdetail/1134117
per capita income calculations from FY2030 onwards. Velázquez also asked for an exclusion from the statutory cap or fixed block grant, starting in 2025. These Medicaid conditions will establish state-like treatment for the territory; however, the suggestion that higher FMAP matching rates were subject to Puerto Rico’s efforts to expand the Medicaid program.

The bill did not pass the Republican-led Congress. Still, numbers show that the USFG augmented the initial budget temporarily on several occasions despite a lack of support for Congresswoman Velázquez’s bill. The increase in healthcare funding in Velázquez’s bill is also an initiative within the Biden Administration’s agenda for Puerto Rico which plans to increase the allotment to $3.6 billion and the federal Medicaid match to 83%. Therefore, Velázquez’s recommendations continue to validate a request to stabilize Puerto Rico’s healthcare system and help its citizens who live in poverty to access health coverage.

As stated by Puerto Rico’s Governor Pierluisi, “if Puerto Rico was treated as a state for purposes of Medicaid, … the [island’s Medicaid] burden will be as little as 13 percent.” An immediate and permanent increase in FMAP by 28% and the waiver of the capped allotment will save the Commonwealth a significant amount of the state budget funds and help individuals eligible for the Medicaid program. To determine Medicaid and CHIP eligibility, Puerto Rico’s government applies a local poverty level, which led to an enrollment of approx. 1.5 million individuals (almost 50% of the population).

The Puerto Rico Department of Health (PRDH) and the Puerto Rico Health Insurance Administration (PRHIA) will collaborate to ensure the proper administration of the Medicaid

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52 Ibid 47
54 Ibid 20
program. And on the federal side, the responsibility remains with the Centers for Medicare & Medicaid Services (CMS) within HHS. The management is a joint effort between the territory and the USFG, that must distribute the resources in the most equitable way possible. Effectiveness and efficiency are critical when operating under tight budgets; therefore, the final element of the PROMESA amendment is the creation of an overarching and independent control mechanism. The GAO pointed out concerns about how Medicaid funds are used and if processes comply with regulations.

The PROMESA adjustment proposes a task force focusing on proper allocation and management. The unit will collaborate with the agencies, assist throughout the processes, and oversee the programs to provide transparency and accountability in meeting the federal standards. Although under PROMESA, FOMB provides guidance for the territory’s budget structure and “is tasked with working with the people and Government of Puerto Rico to create the necessary foundation for economic growth and to restore opportunity to the people of Puerto Rico,” the board’s responsibility has a general fiscal focus. It does not account for efficient and equitable process implementation related to the Medicaid program, which the newly created PMCU will deliver.

PMCU will consist of a small team of healthcare administration professionals and finance specialists selected by the USFG and the Commonwealth. The unit will work on the administrative efficiency, optimization, and compliance of the Medicaid program. The cost for

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57 Ibid 57
PMCU will be initially covered by the administrative expenses under the general Medicaid budget. However, cost claims will be sent to HHS, which will reimburse Puerto Rico under the Medicaid Integrity Program (MIP) and under Innovation and Equity Initiatives. PMCU will coordinate with CMS as they will put a stronger focus on Medicaid in Puerto Rico.

Providing additional funding and simultaneously working towards an improved Medicaid framework will allow the Puerto Rican government to save general revenues allocated toward the program and assist in debt recovery as the government might utilize saved revenues otherwise. The combination of the new PROMESA elements will address the immediate need for financial support and bolster Puerto Rico’s budget by adding much-needed financial resources permanently and at the same time work on ways to maximize their Medicaid funds. The new approach will complement the enacted PROMESA, which oversees the island’s debt management and restructuring procedures.

Because PROMESA was signed into law by former President Obama, amendments to PROMESA require Congressional authorization. As stated in Article 1, Section 159 of the Constitution, “all legislative Powers herein granted shall be vested in a Congress of the United States, which shall consist of a Senate and a House of Representatives.” Under Article V, Congress can propose amendments to laws.60 This proposal should be authorized through a two-third majority vote in the House of Representatives and the Senate. As the Majority Leader of the Senate, you are a pivotal figure in Congress, and you can introduce this proposal and influence the members to act on it. Once it passes Congress, the PROMESA law amendment will

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go to President Joe Biden for his signature. Under the Territory Clause\textsuperscript{61}, Puerto Rico will adopt the revised legislature and incorporate it into its operations and its budget. Nevertheless, a budget proposal will be presented to appointed FOMB for approval which closely monitors the debt restructuring efforts.

V. POLICY ANALYSIS

This proposal aims to free up general funds budgeted for Medicaid and should assist the Puerto Rican government to avoid further entanglement with the public debt build-up. Puerto Rico’s unsustainable Medicaid funding cannot be separated from the approach to ensure general debt sustainability. Puerto Rico heavily relies on federal funding for the Medicaid program and providing more resources directed to health care (approx. $2.5 billion more annually) will shift the health care expenses toward the general fund. Puerto Rico’s share will decrease notably, and an ongoing commitment with open-end allotment will allow Puerto Rico to focus its general revenues on repayment of outstanding obligations. With this plan to provide more Medicaid subsidies, the island can be compared to a state which expanded under the Affordable Care Act, becoming eligible for additional federal revenues.

According to the Robert Wood Johnson Foundation\textsuperscript{62} “expansion states have experienced budget savings” and “documented higher GDP, increased state revenue, jobs, and higher growth in health care wages.” The territory necessitates all these factors to maintain a balanced budget. Also, the Commonwealth Fund\textsuperscript{63} demonstrated a multiplier effect of increased

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federal Medicaid revenue, outcomes that help state economies in various areas. Figure 2 exhibits an example of the interconnectivity between entities and stakeholders and how they are impacted by Medicaid spending.

Figure 2. Flow of Medicaid Dollars Through a State Economy

Flow of Medicaid Dollars Through a State Economy: An Example

As shown in the visual, although the federal injections are directed toward health care services and, in this case, Medicaid, the spending produces income and other opportunities for businesses outside of the Medicaid system and triggers direct, indirect, and infused effects. Therefore, more federal funds will yield larger increases in Puerto Rico’s national income than the money initially spent. Important to mention are also Puerto Rico’s savings of Medicaid share that come with a higher FMAP, which will immediately stimulate the economy beyond the healthcare sector.

64 Ibid 21
In a report on Medicaid Financing and Expenditures\textsuperscript{65}, the Congressional Research Service notes that “Medicaid expenditures account for a significant and growing portion of total health expenditures in the United States” and further adds that the spending level is “influenced by economic, demographic, and programmatic factors.” The Commonwealth is in a financially unstable position and records extremely high poverty rates and the islanders rely on federal and municipal aid and safety nets. Therefore, programs like Medicaid, which cost the island a sizeable portion of its budget, are profoundly important to the financial future of Puerto Rico.

Although the USFG supplemented the territory temporarily with additional Medicaid funds and adjustments to the Medicaid program during the natural disaster crisis and the pandemic, funds were a temporary funding stream and are almost depleted. The Center on Budget and Policy Priorities\textsuperscript{66} outlines that “short-term funding solutions don’t provide the stable adequate funding needed to provide Medicaid coverage,” and also the Kaiser Foundation explained that “temporary funding measures would not address the long-term Medicaid financing issues.”\textsuperscript{67} Thus, the territory lacks a permanent and feasible solution. As of January 2022, the approved block grant for 2022 was $392.5\textsuperscript{68} million, back to its historical levels, and the federal matching rate is subject to return to its original rate for territories (55%). Yet, the CMS in the Department of Health and Human Services (HHS) requested a subsidiary $2.9 billion\textsuperscript{69} for Puerto Rico’s disposal in 2022 under Section 1109(g) of the Social Security Act,

\textsuperscript{66} Ibid 51
which is also the baseline for FOMB’s budget projections towards sustainable debt repayments.70

Nonetheless, the GAO is not aligned with CMS’s interpretation of Section 1109(g) of the Social Security Act and questions their cap amount. GAO71 stated that the policy question of federal Medicaid funding “is clearly a matter of Congress” and further adds that “our conclusion is one of statutory interpretation and the plain meaning of the language of the statute is clear.” Without congressional authorization to permanently increase the allotment or upward adjustment to the federal matching rate, the current conclusion could be challenged legally, which means that Puerto Rico could face another loss in resources for the Medicaid program, federal funds that were part of the forecast assuring fiscal sustainability.

Puerto Rico’s expected federal Medicaid funds are around $2.9 billion72 annually and growing. If the federal government cuts funding, the Commonwealth must supplement with approximately $2.5 billion from their general budget ($2.9 billion minus approx. 400 million historical cap.) The annual allocation of $2.5 billion of general funds toward the healthcare sector will throw Puerto Rico off track and create another financial obstacle as it will take away the fiscal space the increased federal assistance creates. Additionally, lack of resources leads to the Commonwealth’s Medicaid cuts as they need to operate under tight budgets. Potential loss of eligibility and benefits will hurt the already impoverished islanders.

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72 Ibid 65
Figure 3. illustrates Puerto Rico’s allotment scenarios between 2022 to 2026. Although the graph does not give us a long-term view beyond 2026, one can observe the level of impact the Medicaid block grant amount has on the territory. The first and current scenario (scenario 1), in dark blue, shows the block grant of $3 billion in 2022 and grows gradually to approximately $3.2 billion in 2026. The second scenario (scenario 2), displayed by the grey bars, informs about the Medicaid cap if CMS’s interpretation was to be reversed. Here the annual allotment is in the range of $400 million and does not increase. The divergence between scenario 1 and scenario 2 is noticeable.

Figure 3. Puerto Rico’s Medicaid Allotment Scenarios

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Moreover, the lines represent Puerto Rico’s surpluses before the debt service and contribution to the pension trust. The straight line assumes the current level of surplus while the dotted line the surplus under the reversed levels. Although both lines are down-sloping, one can observe that in 2024, under scenario 2, the surpluses decline at a higher rate, and Puerto Rico cannot balance its budget and would occur losses in 2024 and the following years. The visualization shows that a larger block grant is necessary to balance Puerto Rico’s budget.

By authorizing permanent, and therefore structural changes to the territory’s payment and funding mechanisms, as suggested in this memorandum, Puerto Rico will follow the path of scenario 1. Going along with the forecast, as demonstrated with scenario 1, the Commonwealth will be able to meet its obligations. Nevertheless, the current funds are not established by binding laws and regulations, creating a somewhat uncertain future for the Medicaid program and Puerto Rico’s finances. Further, the present conditions do not call for an increase in the FMAP rate, which is part of the proposal. Adding all these aspects to the model would improve the outlook and indelibly change the way the territory approaches fiscal planning.

The Kaiser Family Foundation\(^{74}\) reports that “looking ahead, long-term Medicaid financing reforms such as increased federal matching rates, increased spending caps, or elimination of the caps could help the territories, [in this case, Puerto Rico], meet the healthcare needs of their Medicaid populations. Conversely, the expiration of temporary Medicaid funds without new resources to address the resulting fiscal cliff could negatively affect Medicaid coverage and services. Funding in the projected ranges is required in perpetuity to avoid declining conditions in health and other aspects of the island.

**Figure 4.** demonstrates the high dependence on Medicaid compared to the national average and Mississippi, the state with the highest poverty rate (approx. 18.7% vs. 43.4% in PR)\(^76\). 49% of Puerto Ricans depend on Medicaid, twice as much as residents of Mississippi, the poorest state. The infographic further reveals the perception of health care in their economy. Also, here, Puerto Rico reports the highest rate, with 34% of individuals considering their health care as “fair or poor.” Hence, the recommendation of removing the cap and FMAP adjustments will create a more stable environment for Puerto Rico and its residents which could potentially lead to other positive outcomes and have an impact on government finances.

Enhancing FMAP from 55% to 83% is beneficial for the island as it will provide higher reimbursements to the Puerto Rican government and give the flexibility to expand the Medicaid program instead of minimizing eligibility and the number of beneficiaries, limiting services to the low-income citizens, and reduce payment rates for providers. Reducing funds for programs such

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as Medicaid could result in Puerto Ricans’ outmigration, seeking health services and job opportunities in the healthcare sector on the mainland.

HHS\textsuperscript{77} noted that “physicians have been leaving Puerto Rico” and “evidence clearly indicates a shortage of specialists, and anecdotal evidence suggests a significant emigration of healthcare professionals to the U.S. mainland.” Outmigration is likely to accelerate Puerto Rico’s fiscal issues. It brings consequences such as brain drain, loss of tax-payer dollars, and shifts Medicaid costs to other states, which the federal government compensates with higher matching rates at no fixed allotment. The benefit of the FMAP increase and further elimination of the capped amount would be the immediate and long-term aid the territory would receive, avoiding financial pressure and the resulting fiscal downturns governments would experience otherwise. Conversely, higher funding also allows for mismanagement.

In a Risk Assessment Report\textsuperscript{78}, it was “determined that the risk of improper Medicaid program payments in Puerto Rico could be increased because there have been no recent reviews of Puerto Rico Medicaid program payments performed by the CMS and because Puerto Rico’s Medicaid Management Information System (MMIS) has not been fully implemented.” Improper training of healthcare professionals and understaffing add another layer to the fragile Medicaid program. Other weaknesses are eligibility determination, overpayment to providers, and contract fraud. For example, in 2020, a $38\textsuperscript{79} million contract was awarded to a small organization that does not have a medical background but has political and financial connections. According to the Kaiser Commission on Medicaid and the Uninsured\textsuperscript{80}, around 1.6


\textsuperscript{79} Ibid 78 page 8

\textsuperscript{80} Ibid 6
% of total spending on Medicaid Administration is lost due to fraud and abuse. With an annual Medicaid budget of $2.9 billion, there is a potential loss of $46 million in the area of fraud, waste, and abuse alone, each year. This money could be saved and distributed amongst the agencies that are most distressed.

The proposed PMCU is a necessary requirement to consolidate the efforts of the various organizations that already focus on these areas. PMCU will act as a first-line prevention unit, focused on finding fraud, waste, and abuse rather than enforcement. However, this unit comes at a high financial cost to both the USFG and the people of Puerto Rico, who would undoubtedly not support such a unit, as seen in the case of the FOMB. 81 Although one component of the proposal suggests establishing PMCU, which would work towards the improvement of accountability, integrity, effectiveness, and efficiency of the Medicaid program structure, their efforts may be seen as redundant because several entities already exist using the same approaches to the same end.

HHS’ 2022 budget for MIP is $87.1 million. 82 HHS works closely with the Department of Justice (DOJ) and the HHS Office of Inspector General (OIG) to address fraud, waste, and abuse issues. HHS states that “CMS uses the funds [under MIP] to provide technical support to states and contracts with eligible entities to execute activities such as agency reviews, audits, identification of overpayments, and education activities.” In 2022, the submitted HHS budget for Innovative Center Obligations is $1.168 billion. 83 Also, a budget of $25 million is available for efforts to improve health equity. 84

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81 Ibid 31
83 Ibid 82 page 99
84 Ibid 82 page 104
Regarding the island’s initiatives, Figure 5 provides a detailed breakdown of the Medicaid Program Organizational Structure and its responsibilities. There are several hierarchies in place to ensure the proper use of Medicaid funds, and Puerto Rico has already implemented a controlling mechanism. Nonetheless, the cost is covered under the island’s general Medicaid budget and the healthcare system remains fractured due to a lack of collaboration. PMCU would be financed by the federal government’s initiatives, which would liberate resources the Commonwealth could utilize in other areas and for outstanding obligations.

Figure 5. Puerto Rico Medicaid Program Organizational Structure

Although the PMCU will have a focus on the Medicaid issues at hand, the task unit will not be able to deliver outcomes immediately. Proper research is lengthy and labor-intensive. Also, the task unit could have “deep-seated disagreement about how to handle the issue” or

85 Ibid 82
“group meetings may also be slow and unproductive.” The situation in Puerto Rico requires immediate results and building a new task force aimed at long-term goals will inevitably be counterproductive to the current needs of the territory. There will also undoubtedly be contention with the issue of staffing given Puerto Rico’s distrust for USFG after the initial PROMESA process.

PMCU will deal with Medicaid weaknesses but would disregard the actual root causes of the underfunded program. Therefore, the members of the PMCU must be skillful in both the healthcare system and the economic conditions of the island. Finding such individuals within both governments may be challenging, given the spectrum of requirements needed to execute the tasks within the unit. Another major disadvantage of this proposal is the implementation under PROMESA.

According to the PROMESA, Section 209: Termination of Oversight Board (OB), “the OB would terminate when the OB finds that the territorial government has access to short-term and long-term credit markets at reasonable rates of interest; and achieved balanced budgets for four consecutive years,” which would mean that the authorized Medicaid changes could potentially be compromised. Once the island’s government establishes fiscal stability with the help of alterations to the current Medicaid program’s financial policy, there is no guarantee that Puerto Rican leadership will continue to stay on a sustainable path. Even though increased funds for the Medicaid program will support maintaining balanced budgets, as a territory, and in a vulnerable geographic location, the proposed recommendation cannot prepare the Commonwealth for future crises.

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Finally, a significant disadvantage is that Puerto Ricans do not pay federal income taxes. Yet, this proposal asks for a considerable allocation of federal taxes to be allocated towards the territory. So, simply stated, the federal government will spend resources without collecting additional revenues. This proposal costs the USFG approximately an additional $2.5-3 billion in Medicaid funds annually, but it cannot collect federal income tax revenues as in other states. In an analysis on statehood, GAO\textsuperscript{89} concluded that Puerto Rico would pay federal income taxes in the range of $2.2 billion to $2.3 annually if admitted as the 51st state. Although the focus of this proposal is debt sustainability through Medicaid funding and not statehood admission, it does ask for state-like treatment, thus, allowing for a cost-benefit comparison. As such, much of the federal funding outlaid to Puerto Rico is a cost to the federal government without a fiscal benefit.

**VI. POLITICAL ANALYSIS**

Both parties recognize Puerto Rico’s financial disarray, but discussions for structural changes have not found bipartisan conclusions. Nevertheless, PROMESA was a collective approach to restore the Commonwealth’s financial stability, and an appointed task force consisting of Republican and Democrat officials believed that “an equitable and sustainable legislative solution to the financing of Puerto Rico’s Medicaid program should be enacted”\textsuperscript{90} despite healthcare policy disagreements. They further added that “while it would be wrong to attribute Puerto Rico’s annual deficits and accumulated debt solely or even mainly, to the disproportionate burden it bears in financing its Medicaid program, it would also be wrong to


deny that this funding disparity has been a meaningful factor contributing to Puerto Rico’s fiscal condition.”91 Several lawmakers in both parties understand the necessity for systematic changes, and Puerto Rico’s economic and social points remain on their legislative agenda.

While in the Senate, you previously introduced “legislation to eliminate disparities in Puerto Rico’s Medicare & Medicaid Program,” to provide more equitable federal healthcare funding in US territories’, stating that “Puerto Rico should be offered the same treatment under federal health program as states.”92 Your support for Puerto Rico’s Medicaid program continued, and during the Trump Administration, you announced to return to fully addressing the island’s healthcare funding issues.93

This proposal is a new opportunity to revisit Puerto Rico’s barriers to economic sustainability. Currently, your term runs until 2023, with strong projections for re-election on November 8, 2022. You won in a landslide decision in your last election with over 70% of the vote.94 At the federal level, the Executive branch and the Congress are presently in the hands of Democrats, and President Biden has proven to be an ally, given his historical stance on Puerto Rico’s economic and political issues.

The Biden Administration introduced the BBB plan in 2021, which included adjustments to Puerto Rico’s Medicaid program. The bill proclaimed an allotment increase to $3.6 billion and the FMAP to 83%. There is a clear indication that the Biden Administration aims to assist the territory with additional funds for the healthcare sector and sees structural changes to the

91 Ibid 90 page 19
Medicaid policy as necessary to keep the island’s economy afloat. Although the BBB did not pass in Congress, submitting a separate proposal supporting Puerto Rico’s healthcare policy could gain the majority votes in the House and the Senate. Democrats and Republicans are working towards healthcare equity in the territories.

The Republican Resident Commissioner Jennifer González-Colón introduced H.R.230695 – Puerto Rico Medicaid Act of 2019 in the House, seeking to increase Medicaid funding. Another bipartisan bill, H.R. 440696, asked for additional resources for Medicaid, and a few legislators recognized Puerto Rico’s need for a sustainable solution to the Medicaid program in order to avoid financial shortfalls. In “a letter to Senate Committee on Finance, Chairman Ron Wyden (D-OR) and Ranking Member Mike Crapo (R-ID), [Republican and Democrat Senators are] calling for a long-term solution to Puerto Rico’s Medicaid underfunding.”97

Although there is some sponsorship on fundamental shifts to the territory’s Medicaid budget deficiency, generally, Republican officials do not support increases or expansions to Medicaid. An analysis conducted by the UC Berkeley School of Public Health98 noted that Republican-led states do not favor providing extended Medicaid benefits (towards more low-income citizens or by covering more services). Considering that Republicans are not welcoming Medicaid in several of the red states, it is questionable if there will be enough support for much higher funding for Puerto Rico, an island with a high percentage of Medicaid beneficiaries. In a

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survey on Federal Medicaid funding parity for territories, only 50%\(^99\) of Republican voters supported adjustments to territories’ public health insurance programs. With the midterms approaching, Republican sponsors might be hesitant toward a bill proposed by a Democrat unless it contains a provision to pay for any increase or major structural changes to Medicaid.

Also, in a letter\(^{100}\) addressed to HHS, Republican Senators expressed concerns and the lack of transparency and accountability with federal Medicaid funds. The Senators brought to attention that “there are, of course, difficulties in assessing ‘equitable’ Medicaid funding for Puerto Rico, including the fact that while Medicaid is funded out of the general fund of the United States, individuals in Puerto Rico do not participate in the federal personal income tax system, which helps finance the general fund.”

As a matter of political practice, the GOP has advocated for the wealthy through legislation and is working slowly toward dismantling and retrenching the basic structure of Medicaid.\(^{101}\) For years, Republican policymakers tried to repeal Medicaid expansions and convert the program into a block grant, minimizing benefit enhancement and eligibility.\(^{102}\)\(^{103}\) One of the arguments that conservatives may raise is that the federal share for Puerto Rico is not returned through tax revenues, which could be perceived as inequitable. Although equitable access to health care is the goal, state-like treatment seeks equity and equality but mandating...


federal income taxes on the Commonwealth to establish a shared-risk shared-cost mechanism would contradict the rules of their territorial status.

However, in the revised legislature, federal resources would be controlled tightly with an effort to maximize tax dollars. Monitoring and responsible administration are important elements of this proposal as it incorporates changes under PROMESA and implements conditions to the resources, thus taking autonomy away from Puerto Rico. The Congressional Republicans voted for fiscal oversight throughout the debt restructuring process and “see the strong control board as crucial to the territory’s recovery.”

Figure 6.105 displays the main stakeholder groups involved in the decision-making under PROMESA and shows their viewpoint on the bill. The GOP and creditors showed strong support for an oversight board and were resistant to debt restructuring. At the same time, Democrats and Puerto Rican Leaders approved restructuring efforts and favored no or limited control over finances.

**Figure 6. Viewpoints on Debt Restructuring and Fiscal Oversight**

<table>
<thead>
<tr>
<th>Debt Restructuring</th>
<th>Fiscal Oversight</th>
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<tbody>
<tr>
<td>Creditors</td>
<td></td>
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<tr>
<td>Puerto Rican</td>
<td></td>
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<tr>
<td>Politicians</td>
<td>Prefer no control board or a limited one at least partially elected by Puerto Ricans</td>
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<tr>
<td>Comprehensive</td>
<td>Support a strong, unelected FFCB</td>
</tr>
<tr>
<td>bankruptcy or other form of restructuring</td>
<td></td>
</tr>
<tr>
<td>Republican</td>
<td>Support a strong, unelected FFCB</td>
</tr>
<tr>
<td>Administration</td>
<td>Support a control board that respects “Puerto Rican sovereignty”</td>
</tr>
<tr>
<td>Many opposed to restructuring unless absolutely necessary</td>
<td></td>
</tr>
</tbody>
</table>


105 Ibid 101
Since the collective response was the FOMB with control over Puerto Rico’s budgets, Republican officials did not argue the decisions made regarding the island’s finances, proving that their attitudes towards tight oversight and decreased autonomy are unchanged. Therefore, the newly proposed PMCU would most likely not receive objections from the House and Senate Republicans. However, the PMCU could be opposed by Puerto Rico and the general public.

Data for Progress\textsuperscript{106} recently conducted a survey on PROMESA. Key takeaways are that “Americans [islanders and mainlanders alike] overwhelmingly oppose the federal government’s takeover of Puerto Rico’s finances,” and oversight is unsupported and seen as undemocratic. But about 65% of voters “support various reforms so Puerto Rico can manage its debt more sustainably.” The conditions of this proposal might find opposition from the general public as they do not favor tight government controls. While the recommendation expands the benefits to the territory, it does it under a law that has gained criticism and a negative stigma since it was authorized.

Finally, the dimension of Puerto Rican views and their trust in its government play a significant role when implementing transformative changes. A survey\textsuperscript{107} revealed that the islanders identified the healthcare system, corruption, and a lack of government transparency as major issues. This proposal introduces improvements to the three areas, which should appease those Puerto Ricans who distrust their institutions. Although, at present, Puerto Ricans do not have congressional representation and a voice in federal elections, a change in their territorial status is debated intensively among all stakeholders. Supporting Puerto Rico in any aspect will win votes on the mainland and in the future should statehood be realized.


VII. RECOMMENDATION

The proposal of addressing debt sustainability through strengthening one of the principal budget cost drivers is a feasible solution for Puerto Rico. Federal support is necessary to overcome Puerto Rico’s liquidity crisis and economic decline, and the Commonwealth, because of its territorial status, has been in a dire situation for decades. The US territory, faced with unsettling challenges, such as extremely high poverty rates, poor infrastructure, and a debt burden that the island’s government accumulated over the years, deserves a fundamental and sustainable response. It is important to point out that the liquidity issues and the accumulated debt result from the USFG’s poor policy choices implemented on the island, Puerto Rico’s fight during recessions and crises, and mismanagement by the territory’s governing officials.

As described by a group of economists in a document known as the Krueger Report\textsuperscript{108}, Puerto Rico’s “debt cannot be made sustainable without growth, nor can growth occur in face of structural obstacle and doubts about debt sustainability.” The authors add that “the debt crisis is not just a fiscal one but also reflects structural problems that held back growth – both need to be tackled together.” We have observed that with the initial PROMESA, the USFG mainly tackled Puerto Rico’s fiscal crisis emphasizing the financial aspect rather than the root causes. Structural reform was not favored as a bipartisan solution. While this proposal does not discuss a growth strategy, it calls for a structural change, which will address budgetary pressure and healthcare system distress.

Changes to the Medicaid system and an upward adjustment of federal funding will create much-needed relief to the island’s budget. By giving Puerto Rico additional provisions in the amount of approx. $2.5 billion annually will free up capital required to meet the ongoing

obligations, and for that reason, debt sustainability is secured to a great degree. This solution will show immediate impact as the government can count on more robust federal assistance and thus incorporate higher revenues in their debt sustainability planning. Puerto Rico will observe instant and long-term results of more federal aid and the realities that emerge from a healthier citizenry and economy.

Medicaid plays a vital role in fiscal recovery. Evidence shows that increased federal funding has a multiplier effect and can generate economic benefits for citizens and the state economy in general. For Puerto Rico, permanent FMAP revisions and an open-ended block grant will release a guaranteed influx of federal revenues to address challenges in the island’s ambiguous and fragile environment. The Commonwealth will be able to stabilize its healthcare system and repair its long-lasting financial issues in Medicaid and beyond.

Although the proposed PMCU, one elements of the recommendation, might have disadvantages, such as slow progress, potential disagreements, or the perception of being irrelevant due to processes already in place, the task force has a more targeted goal to minimize mismanagement and ineffectiveness. It provides an additional control apparatus the federal government might find necessary when distributing more taxpayer dollars. Nevertheless, it is understood that systematic accountability and transparency are crucial factors when spending public resources.

Despite the gains this proposal provides, it comes at an annual cost for the USFG and the mainland residents, but not for the Puerto Rican taxpayer since they are exempt from paying taxes that are used to cover the federal Medicaid expense. While the argument is strong, we must see “the bigger picture.” In a struggling Puerto Rico without improvement and growth in sight, islanders will be motivated to relocate to one of the states in the US that offers more opportunities and a better standard of living. As US citizens, Puerto Ricans are entitled to do so.
Consequently, Puerto Rico’s economy will weaken, and the USFG will incur a cost as it will support Puerto Ricans elsewhere in the US at a much higher rate.

In summary, the benefits of the proposal outweigh the cost. Under a revised PROMESA, making Medicaid more equitable is a functional approach to maintaining debt sustainability. With a House and Senate in the hands of Democrats, several Republican officials supporting diverse political and economic matters regarding Puerto Rico, and a Puerto Rican Governor outlining the need for Medicaid equity, this proposal, with your support, has an opportunity to proceed through Congress and deliver the long-promised financial relief. Therefore, I do recommend this proposal.
CURRICULUM VITAE

Magdalene Bramlett was born in Czeladz, Poland. At the age of 9, she moved with her family to Germany. In 2016, Magdalene relocated to the USA to join her husband, a US Army Intelligence Officer. Before moving to NJ, in Germany, she worked for international organizations and in her latest position as a project manager in the finance industry. Magdalene earned her Bachelor of Science in Global Enterprise Management and a Certificate in Social Entrepreneurship from the University of Delaware. She recently accepted a position as a Statistical Analyst for NJ Courts. She supports the Quality Assurance and Analytics Unit in the Department of Probation Services. Magdalene is interested in data analysis, racial equity, and community development.