



Puerto Rico needs the right kind of financial control board

By Arturo C. Porzecanski, February 24, 2016

As one of the [earliest proponents](#) of a federal oversight board to manage Puerto Rico's grave fiscal situation, I find it reassuring to hear that more and more members of Congress are now inclined to legislate such a board into existence.

The discussion has shifted to the all-important details: What goals should the board pursue? How broad a mandate should it be given? What specific powers should the board have? And indeed, the proverbial Devil will be in the details.

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U.S. Treasury Counselor Antonio Weiss is to be a witness at a U.S. House of Representatives Natural Resources Committee hearing later this week on Puerto Rico, after which lawmakers are expected to begin drafting legislation. However, unless there has been a sudden change of heart in the Obama administration, Weiss will merely reiterate [the official view](#) that Congress should provide "independent fiscal oversight while respecting Puerto Rico's autonomy," and that territories like Puerto Rico be provided "with a legal framework that allows for a comprehensive restructuring" of the island's debt obligations – a "Super-Chapter 9" mechanism that would nullify even the creditor rights enshrined in Puerto Rico's own Constitution.

Independent fiscal oversight that respects Puerto Rico's autonomy is precisely the kind of light-handed approach favored by Governor Alejandro García Padilla, the captain of the ship who is responsible for its taking on so much water that it is in imminent danger of sinking. He recently persuaded his own legislature to set up just such a toothless oversight board in Puerto Rico, but he hasn't nominated its members because he knows that such an enterprise is futile: it has no credibility. The same would be true of some kind of blue-ribbon committee established by Congress to operate with the advice and consent of the island's elected authorities. What the circumstances warrant, instead, is a federal intervention into the fiscal affairs of Puerto Rico, and therefore a strong financial control board like that imposed in the mid-1990s on another territory – the District of Columbia.

What goals should the board pursue? The ultimate goal should be to restore Puerto Rico's access to the municipal bond market on terms and conditions which are sustainable – namely, borrowing costs in the low single digits and maturities measured in many years, if not decades. The reason is that it behooves nobody, least of all its proud inhabitants, for Puerto Rico to become a permanent ward of a federal government which will have to provide the financing that the bond market would no longer deliver. The Commonwealth must stop running budget deficits and start achieving operating surpluses, for which purpose the board should have the authority to

design and implement a comprehensive reform of the island's public finances – starting with its crooked accounting and byzantine structure.

How broad a mandate should the board be given? Achieving a lasting improvement of the Commonwealth's finances depends on a series of revenue-raising, expenditure-cutting, and privatization measures; a new compact with the federal government, so that the island will receive its fair share of Medicaid and other transfers; and new incentives to investment and job creation, for which purpose Puerto Rico would best be exempted from various federal mandates (e.g., the minimum wage and the Jones Act) which conspire against economic growth. Therefore, the financial control board should have broad authority.

What specific powers should the board have? Given the magnitude of the problem, Congress should vest the control board with wide-ranging powers to approve or reject all government budget and financial plans; enact revenue- and expenditure-side reforms and measures; mobilize and monetize government-owned assets; authorize all additional borrowing; and make key managerial appointments. These are largely the powers that were vested in the financial control board of the District of Columbia [with tremendous success](#).

What about the power to repudiate debts through bankruptcy? According to a recent [debt restructuring proposal](#) put forth by the government of Puerto Rico, achieving a sustainable debt burden supposedly requires that the millions of bondholders who purchased the island's obligations grant forgiveness of principal and interest payments ranging, in present-value terms, from 30 percent to as much as 60 percent of what they are owed.

The power to impose this kind of damage onto a largely retail investor base through a "Super-Chapter 9" mechanism should not be granted. The debt forgiveness demanded by the authorities in San Juan reflects their political imperative to shun the design and implementation of tough fiscal reforms during an election year. The public-sector labor unions, which are dominant in Puerto Rico, have made it crystal clear that they will turn against any politician who asks them to sacrifice. That may be a good enough reason for the island's political class to want to abdicate its responsibilities to bondholders, and even to violate the Commonwealth's constitutional protections, but surely the U.S. Congress can see through this and will avoid setting a terrible precedent for the U.S. municipal debt market.

Prof. Porzecanski is the director of the International Economic Relations Program at American University's School of International Service.

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