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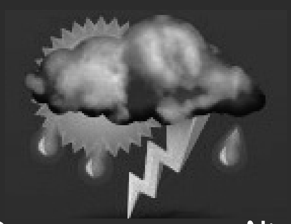
Today's
weather



Day	Night
High	Low
87°F	76°F
Precip 80%	Precip 40%
T-Storm	T-Storm

Wind: From ENE at 11 mph
Humidity: 77%
UV Index: 11 - Extreme
Sunrise: 6:13 AM
Sunset: 6:20 PM

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International Economist Says GDB at Center of PR's Fiscal Problems

By EVA LLORENS VELEZ
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Economist Arturo Porzecanski has made public a paper that states that the Government Development Bank (GDB) is at the heart of Puerto Rico's fiscal problems.

"The time has come for Puerto Rico to start addressing its economic growth and competitiveness challenges in order to regain fiscal and financial stability – and avoid the worst-case scenarios, for the sake of the Government Development Bank and the Commonwealth at large," he said.

The Uruguyan economist urged a restructuring of some of the entities that have the most debt with the bank.

The GDB's most immediate problem is that the Puerto Rico Highway and Transportation Authority (PRHTA) accounts for nearly one-fourth of its loan book, he said.

"A bill currently in the Senate, if passed into law, would channel PRHTA revenues to the PR Infrastructure Financing Authority [PRIFA] for it to issue new bonds whose proceeds would pay off the GDB loans," Porzecanski said. "If this bill were to become law, it would immunize the GDB from taking a [large] cut."

He added passage of the measure is essential for the credibility of what he called a "ring-fencing effort" that would protect the government bank from the accumulating debt of agencies and public corporations.

"The successful sheltering of excluded government entities by definition also significantly reduces the GDB's transfer risk," he said.

In the paper, Porzecanski, an expert in international finance, emerging markets and Latin American economics, says the GDB's role has evolved significantly over time, and it is now the financial heart of the commonwealth. In the 1950s, two-thirds of the bank's total loans granted went to private companies – everything from laundries to car-repair shops, drugstores, milk-processing plants, and furniture factories.

Starting in the 1970s, however, the GDB began to spawn a series of subsidiaries – like the Puerto Rico (PR) Municipal Finance Agency, PR Development Fund, PR Housing Finance Authority, and PR Tourism Development Fund – while successive governments were setting up other state enterprises, mainly the PR Electric Power Authority (PREPA).

"The GDB's financial support for these entities has been such that, by mid-2014, virtually all (99.6 percent) of the bank's nearly $9 billion in loan exposure was to public-sector obligors, with the troubled PRHTA alone accounting for $2 billion, or nearly one-quarter, of total loans," the economist said. "On the liability side of its ledger, virtually all (99.1 percent) of its $5.6 billion in deposits belonged to state-owned enterprises, with an additional $4.7 billion of funding provided by GDB notes placed with investors – two funding sources which are subject to rollover risk. The GDB serves as the principal source of short-term liquidity for the Commonwealth and its many entities."

Porzecanski, who worked for decades on Wall Street and is now Distinguished Economist in Residence at American University in Washington, D.C., said the GDB's corporate governance and image have deteriorated over time. The bank historically has been able to attract well educated, highly competent investment and loan professionals to its ranks, he said.

"For a long time, the GDB was considered to be a technocratic institution relatively insulated from the political world, so much so that neither its top appointed officials nor its seven-member board of directors has been subject to Senate confirmation hearings. In more recent times, in contrast, the GDB has had very short-lived chief executives and an abundance of interim leadership," he said.

Porzecanski said the administration of Gov. Sila María Calderón (2001-2004) marked a turning point for the GDB, when she and the Puerto Rico Legislature at the time enacted laws to force the GDB to pay a large portion of its capital ($500 million) as a one-time dividend to the

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From page 3 government's coffers, and to provide a $500 million loan to fund a perpetual trust to attack poverty in the commonwealth.

"That event marked an important change in the way the political class and society at large began to view the GDB: it came to be regarded as the government's 'piggy bank,'" he said.

The GDB was also the target of a caustic ad that ran last week in the stateside publications Politico and The Wall Street Journal, calling on the U.S. Congress to audit the GDB.

The ad placed by the American Future Fund (AFF) – the same conservative organization that also ran an ad likening the administration of Gov. Alejandro García Padilla to the government of President Nicolás Maduro in Venezuela and accusing the government in San Juan of promoting corruption – accused the GDB of operating outside the reach of Washington regulators and allowing the governor to bankroll a rogue government.

"Governor [García] Padilla and his cronies control a secret slush fund known as the Government Development Bank," the ad read. "To unwitting investors, governor [García] Padilla sells the GDB as a safe place to invest, even if it has amassed billion in debt."

Porzecanski notes that the GDB is by far the largest bank in the United States that is neither a member of the Federal Reserve System nor overseen by the FDIC. Puerto Rico's commercial banks are supervised by both the Federal Reserve Bank and FDIC, and two of them (Banco Popular and First BanCorp.) received TARP monies in the wake of the mainland's financial crisis.

The GDB, by contrast, is regulated only by the Office of the Commissioner of Financial Institutions of Puerto Rico (OCIF by its Spanish acronym) – and OCIF's oversight has not been strong, the economist said. The GDB is audited by the commonwealth Comptroller's Office and by its external auditors (currently KPMG). The Comptroller has authorized external audits over the years, but these have been limited to general operations and procedural matters.

"Since the GDB is vulnerable to a deepening of the crisis in the Commonwealth, and it does not have recourse to a lender of last resort, it poses a systemic risk to the financial system and economy of Puerto Rico," Porzecanski said.

Puerto Rico has been in a slump since 2006, and economic activity has continued to contract and remains generally depressed, with no signs that a bottom has been reached. The creditworthiness of the commonwealth and of its leading bank – the GDB – will thus likely remain quite shaky for many months to come, the economist added.

Despite the bold economic recovery agenda over the past year, question marks still linger over the willingness of the authorities to embark on growth-promoting structural reforms, he said.

"The Recovery Act, which facilitates the restructuring and reduction of liabilities without ensuring the adoption of new business models, came at the urging of the labor unions in the public sector because they were clamoring for a shared sacrifice with creditors – meaning, bondholders," Porzecanski said. "While the current crisis should be providing an opportunity for economic reform, the current administration appears timid and is busier playing defense rather than offense."

FDIC Mum on Doral's Fate as Gov't Presses Case Against Tax Refund

By EVA LLORENS VELEZ
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As the government insisted last week that it submitted enough evidence to prove that Doral Bank is not entitled to a $230 million tax refund, the Federal Deposit Insurance Corp. (FDIC) is not saying whether it will make the move to take over control of the bank.

Federal regulators are forcing Doral Financial to revise its capital plan, prompting the bank to make attempts to increase its Tier 1 capital and sell assets. Recently, the bank moved to sell more than $400 million in loans.

The FDIC in May determined that 43 percent of the assets the bank had been using to calculate its capital ratios no longer can be used for that purpose. The FDIC told Doral it can't include tax receivables from the government of Puerto Rico. The receivables accounted for $289 million of the bank's roughly $679 million of so-called Tier 1 capital as of the end of last year.

The FDIC said Doral was not allowed to accept or roll over any brokered deposits unless it has been granted an FDIC waiver. Brokered deposits – or bank deposits sold through brokerages – account for about 18 percent of Doral's funding.

The bank said the FDIC won't consider granting it waivers to accept brokered deposits until it provides revised capital calculations.

The FDIC had virtually given Doral until the end of the summer to put its house in order. However, it has yet to act against the bank.

"We will not comment at this time," the FDIC told the Star.

The bank recently sued the Treasury Department for voiding a 2012 closing agreement in which the agency agreed to pay the bank a $230 million tax refund that could help the bank with its financial troubles. Treasury says Doral did not overpay in taxes and is not entitled to the refund.

On Friday, Justice Department lawyer Claudia Juan proclaimed after a court hearing that the agency has proven its case against Doral.

Justice put Treasury expert Juan Zaragosa on the stand, who pointed out three instances in which Doral falsified information to obtain a tax refund. One of the areas centered on bank revenues.

Former Treasury Secretary Xenia Vélez defended her role in the transaction as she advised on it. She noted that the initial closing agreements made in 2004 and 2006 are not different from the 2012 closing agreement that is in dispute. According to reports, the tax overpayments were made in the early 2000s.

As of press time, Treasury Secretary Melba Acosta was slated to testify, and Superior Court Judge Laureana Pérez Pérez was expected to issue a ruling this week.

Meanwhile, the New Progressive Party in the House requested an investigation into a 2013 closing agreement made with Doral by current officials in which Electoral Commissioner Eder Ortiz allegedly participated. In the agreement, Treasury agreed to give the bank a $56 million credit for a tax overpayment.