

How Can Puerto Rico Restructure Its Debt Obligations and Return Its Economy to Growth?

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Legislative Update

Proposed Puerto Rico Recovery Law

Editor’s Note: This month’s Legislative Update features a summary of the provisions found in the Puerto Rico Oversight, Management and Economic Stability Act (PROMESA), as introduced and amended (as of April 12). The legislation is pending in the U.S. House of Representatives Committee on

Resources. Thanks go to *Sonia Colón and Jorge San Miguel (Ferraiuoli LLC; San Juan, Puerto Rico, and Orlando, Fla.)* for the content of this Update. **abi**

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Comparison of PROMESA as Introduced and Amended (as of April 12)

The Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) (as introduced on March 29); Changes as amended: <i>The Puerto Rico Oversight, Management, and Economic Stability Act (April 12) are in blue italics.</i>	
Title I – Sets Forth the Composition Requirements of the Financial Oversight and Management Board	
101(b) – Composition of Board 101(e) – Composition of Board	<ul style="list-style-type: none"> • The Oversight Board shall consist of five members appointed by the President after consulting with the chairs of the Committee on Natural Resources of the House of Representatives, and the Committee on Energy and Natural Resources of the Senate. • The governor of Puerto Rico and Puerto Rico secretary of state shall serve as <i>ex officio</i> members of the Oversight Board without any voting rights. • The President shall designate the chair of the Oversight Board. • <i>The Oversight Board shall consist of seven members appointed by the President.</i> • <i>Two individuals should be selected from a list of individuals submitted by the Speaker of the House of Representatives, of which one shall have a primary residence or place of business in Puerto Rico.</i> • <i>Two individuals should be selected from a list of individuals submitted by the majority leader of the Senate.</i> • <i>One individual should be selected from a list of individuals submitted by the minority leader of the House of Representatives.</i> • <i>One individual should be selected from a list of individuals submitted by the minority leader of the Senate.</i> • <i>The governor is an ex officio member of the Oversight Board without voting rights.</i> • <i>The voting members shall designate the chair of the Oversight Board.</i>
101(c) – Oversight Board Membership Qualifications 101(e) – Oversight Board Membership Qualifications	<ul style="list-style-type: none"> • Has knowledge and expertise in finance, management, law, or the organization or operation of business or government. • Does not provide goods or services to the government of Puerto Rico nor is related to an individual who provides said goods or services. • Is not an officer, elected official or employee of the government of Puerto Rico or a candidate for elected office of the government of Puerto Rico. • Maintains a primary residence or has a primary place of business in Puerto Rico, provided that this paragraph shall apply to at least two members. • <i>Has knowledge and expertise in finance, management, law, or the organization or operation of business or government.</i> • <i>Is not an officer, elected official or employee of the government of Puerto Rico or a candidate for elected office of the government of Puerto Rico.</i>
104 – Powers of the Oversight Board	<ul style="list-style-type: none"> • Hold hearings, take testimony and receive evidence as the Oversight Board considers appropriate. • Obtain official data from federal or Puerto Rico government entity when deemed necessary. • May issue subpoenas requiring the attendance and testimony of witnesses and the production of books, records, correspondence, memoranda, papers, documents, electronic files, metadata, tapes, and materials of any nature relating to any matter under investigation by the Oversight Board.
107 – Budget and Funding for Oversight Board Operation 107 – Budget and Funding for Oversight Board Operation	<ul style="list-style-type: none"> • Oversight Board may use its powers with respect to the territory budget of the covered territory to ensure that sufficient funds are available to cover all expenses of the Oversight Board. • Oversight Board shall, in the name of the Commonwealth of Puerto Rico, issue bonds or other loan indentures in amounts and maturities sufficient to fund the activities of the Oversight Board for a period of not less than five years. • <i>The Oversight Board shall submit a budget for each fiscal year of operations to the President, House of Representatives Committee on Natural Resources, Senate Committee on Energy and Natural Resources, the governor of Puerto Rico and legislative assembly of Puerto Rico.</i> • <i>The Oversight Board may use its powers with respect to the territory budget of the covered territory to ensure that sufficient funds are available to cover all expenses of the Oversight Board.</i>
109 – Autonomy of the Board	<ul style="list-style-type: none"> • The governor nor the legislative assembly of Puerto Rico shall have no control supervision, or oversight nor can they enact legislation with respect to the Oversight Board. <i>(Provision is number 108 in the H.R. 4900 version.)</i>
109 – Legal Representation 108 – Legal Representation 109 – Ethics	<ul style="list-style-type: none"> • The Oversight Board shall be represented by such counsel as it may select, but in no instance may it be represented by the Secretary of Justice of Puerto Rico. • <i>The Oversight Board shall be represented by such counsel as it may hire or retain so long as no conflict of interest exists.</i> • <i>All members and staff of the Oversight Board shall be subject to (1) the federal conflict of interest requirements described in § 2018 of title 18, U.S. Code; and (2) the financial disclosure requirements under title I of the Ethics in Government Act of 1978.</i>
Title II – Sets Forth the Responsibilities of the Oversight Board	
201 – Development of Fiscal Plan and Budget for Puerto Rico (Provision is called “Approval of Fiscal Plans” in the H.R. 4900 version.)	<ul style="list-style-type: none"> • The government of Puerto Rico shall develop and submit to the Oversight Board a fiscal plan and budget for each fiscal year during the oversight period. • The fiscal plan and budget shall specify the budgets for Puerto Rico for the applicable fiscal year and the next four years (including revenues and expenses on a modified accrual basis for each fund of the government). Among other requirements, it must describe lump-sum expenditures by department by object class, describe capital expenditures, and contain cash flow forecasts for each fund of the government. • The fiscal plan and budget shall meet, among others, the following standards: Beginning with fiscal year 2017, the expenditures of the government for each fiscal year may not exceed the revenues of the government for each such fiscal year; during 2017-18, the government shall make continuous and substantial progress toward equalizing the expenditures and revenues for such years; and the government shall provide for the orderly liquidation of the cumulative fund balance deficit. • The government shall apply sound budgetary practices, including reducing costs and other expenditures, improving productivity, increasing revenues, or combinations of such practices. • During an oversight year, the legislature may not approve and the governor may not forward to the President any budget that is inconsistent with the fiscal plan and budget established for said year.

Legislative Update: Puerto Rico's PROMESA as Amended

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Comparison of PROMESA and H.R. 4900 (continued)

202 – Development of Budgets	<ul style="list-style-type: none"> • As soon as practicable after at least three members of the Oversight Board have been appointed in the fiscal year in which it is appointed, the board shall deliver a notice to the governor and legislature providing a schedule to submit and certify budgets for a certain period. In any case, the period may not be less than one fiscal year following the fiscal year in which the notice is delivered. The governor and legislature shall submit to the Oversight Board a forecast of revenues for the following year to be used in developing the budgets. • The governor shall deliver the budget to the Oversight Board, and the board will approve it and submit it to the legislature if it is a compliant budget. If it is not, the board will provide to the governor a notice of violation with a description of the necessary action and an opportunity to correct the violation within a specified term. If the governor fails to do so, the Oversight Board shall develop and submit to the governor and legislature a revised compliant budget. • The budget for the year immediately following the fiscal year in which the Oversight Board is established is not required to be a compliant budget. • During the fiscal year in which the Oversight Board is established, the board shall have sole discretion in determining whether a budget is acceptable. • The legislature shall submit to the Oversight Board the budget adopted by it within the term specified by the schedule provided by the board. The board will approve it if it is a compliant budget and will issue a compliance certification. If it is not, the board will provide to the legislature a notice of violation with a description of the necessary action and an opportunity to correct the violation within a specified term. If the legislature fails to do so, the Oversight Board shall develop and submit to the governor and the legislature a revised compliant budget. • The Oversight Board shall issue a compliance certification to the governor and legislature if the budget submitted is a compliant budget, or an acceptable budget for the year in which the Oversight Board is established, and it was submitted by the day before the first day of the fiscal year for said budget. If the governor and legislature fail to file said compliant budget, or the budget is deemed acceptable for the year in which the board is established, the budget submitted by the Oversight Board shall be deemed to be approved by the governor and legislature, subject to a certificate of compliance, and will be in full force and effect beginning on the first day of the applicable fiscal year. • The governor shall submit to the Oversight Board quarterly reports describing the actual cash revenues, cash expenditures and cash flows of the government as compared to those in the certified budget. • Upon receipt of the quarterly reports, the Oversight Board shall conduct a review to determine if the actual quarterly revenues and expenses of Puerto Rico are in compliance with the applicable certified budgets. If the board determines that they are not, it shall issue a notice of violation and a description of the necessary corrective measures to the governor and legislature, as well as an opportunity to correct the violation by a date specified in the notice of the deadlines and scheduling. If the governor and legislature fail to correct the violations, the Oversight Board has the power to make appropriate across-the-board reductions in nondebt expenditures to ensure that the actual quarterly revenues and expenses for the government are in compliance with the budget. If the government initiates appropriate measures to reduce expenditures or increase revenues, the board shall cancel the reductions.
203 – Oversight Board Related to Debt Issuance and Restructuring	<ul style="list-style-type: none"> • If the government reaches a voluntary agreement with holders of its debt to restructure the debt in a manner that conforms to the applicable certified fiscal plan, the Oversight Board shall issue a certification to the effect that the voluntary agreement provides for a sustainable level of debt and is in conformance with the applicable certified fiscal plan. The effectiveness of the agreement is conditioned on the Oversight Board issuing said certification. • Within the first six months of the establishment of the Oversight Board, the governor shall submit an audited report to the board documenting all outstanding discretionary tax waiver agreements to which the government is a party. No new tax waiver agreements may be executed without the approval of the Oversight Board.
204 – Development and Approval of Fiscal Plans	<ul style="list-style-type: none"> • As soon as practicable after at least three members of the Oversight Board have been appointed in the fiscal year in which it is appointed, the board shall deliver a notice to the governor providing a schedule for the process of development, submission, approval and certification of fiscal plans, including subsequent revisions. • A fiscal plan shall, among others, provide for estimates of revenues and expenses in conformance with modified accrual accounting standards, ensure the funding of essential public services, provide adequate funding for public pension systems, provide for the elimination of budget gaps in financing and improve the fiscal governance. • The fiscal plan shall cover a period of years determined by the Oversight Board, which shall be of no less than five years. • The governor shall not submit a budget to the legislature unless the Oversight Board has certified the fiscal plan for that year, unless the board, in its sole discretion, waives this requirement. • If the Oversight Board determines that the fiscal plan satisfies all requirements, it shall approve it. If it determines that the plan does not satisfy all requirements, the Oversight Board shall provide to the governor a notice of violation that includes recommendations for revisions to the applicable fiscal plan and an opportunity to correct the violation. • The governor shall revise and submit to the Oversight Board a revised proposed fiscal plan within the time allowed in the notice providing the schedule. If the governor fails to submit a compliant fiscal plan, the Oversight Board shall develop, approve and submit to the governor and legislature a fiscal plan that satisfies the applicable requirements. • If the Oversight Board approves a fiscal plan, it shall deliver a compliance certification to the governor and legislature. If the plan is developed by the Oversight Board and the governor fails to correct, said plan is deemed approved by the governor.

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Comparison of PROMESA and H.R. 4900 (continued)

<p>205 – Review of Activities of Government of Puerto Rico to Ensure Compliance with Approved Financial Plan and Budget</p>	<ul style="list-style-type: none"> • The legislature shall submit to the Oversight Board each Act passed by the legislature during an oversight year. The board will review the act to determine if it is consistent with the applicable fiscal plan and budget. If it is consistent, the board will notify the legislature that it approves that Act and it shall become law. If it does not, the Act shall be null and void and the board shall notify the legislature, provide it with an explanation, and to the extent appropriate, provide the legislature with recommendations for modifications to the Act. • If the Oversight Board fails to notify the approval or disapproval within a 14-day period following the submission of the Act by the legislature, excluding Saturday, Sundays and legal holidays, the Oversight Board is deemed to have approved the Act. The legislature may request the Oversight Board to conduct a preliminary review of proposed legislation. • In the case of any contract or lease that is proposed to be entered into by the government during an oversight year, the governor shall submit the proposed contract of lease to the board, and the governor may not enter into said contract or lease unless the board determines that the contract or lease is consistent with the fiscal plan and budget for the fiscal year. If the legislature must approve the contract or lease, the governor shall submit it to the board only after the legislature has approved it. • If the governor submits a request to the legislature to reprogram any amounts provided in the budget for an oversight year after the budget is adopted by the legislature, the governor shall submit said request to the Oversight Board, which shall analyze its effect on the fiscal plan and budget, and submit its analysis to the legislature. The legislature may not act on the request until it receives the analysis from the Oversight Board.
<p>206 – Restrictions on Borrowing by Puerto Rico during Oversight Year</p>	<ul style="list-style-type: none"> • The government may not borrow money during an oversight year without obtaining a certification from the Oversight Board. • If the Oversight Board determines that the borrowing proposed to be undertaken by the government is not consistent with the fiscal plan and budget, the governor may submit to the board a proposed revision to the fiscal plan and budget. • If the government borrows funds, the funds shall be deposited into an escrow account held by the Oversight Board to be allocated pursuant to the fiscal plan and budget.
<p>207 – Effect of Finding Noncompliance with Financial Plan and Budget</p>	<ul style="list-style-type: none"> • No later than 30 days after the expiration of each quarter of each fiscal year (beginning in 2017), the governor shall submit reports to the Oversight Board describing the actual revenues obtained and expenditures made by the government and comparing these with the most recent projections. If the board determines that there are inconsistencies between external reports and those of the government, it may require additional information from the government to explain inconsistencies. • After requiring additional information from the governor, the Oversight Board shall certify to the legislature, the President, and Congress that the government is at variance with the fiscal plan and Budget unless the additional information explains the inconsistency and such explanation is reasonable and appropriate or the government adopts or implements remedial action, and the Governor agrees to submit monthly reports for such period as the board may require.
<p>208 – Recommendations on Financial Stability and Management Responsibility</p>	<ul style="list-style-type: none"> • The Oversight Board may submit recommendations at any time to the governor, the legislature, the President and Congress on actions the government or the federal government may take to ensure compliance with a fiscal plan and budget or to otherwise promote financial stability, management responsibility and service delivery efficiency. These include the management of the government's financial affairs; the structural relationship of departments, agencies and independent agencies; the modification of existing revenue structures or the establishment of additional revenue structures; and the effects of Puerto Rico laws and court orders on the government. • Within 90 days after receiving a recommendation, the governor or legislature shall submit a statement to the Oversight Board, the President, and Congress that provides notice as to whether the government will adopt the recommendations. If the government or legislature notify that a recommendation will be adopted, it shall include with the statement to that effect a written plan to implement the recommendations that include specific performance measures and a schedule for auditing the government's compliance with the plan. If the governor or legislature notify that a recommendation will not be adopted, it shall include in the statement explanations for the rejection of the recommendation. Further, the Oversight Board may by a majority vote take such action concerning the recommendation as it deems appropriate after consulting with the Committee on National Resources of the House of Representatives and the Committee on Energy and Natural Resources of the Senate. This power will apply with respect to any recommendation made after the expiration of the six-month period following the date of the enactment of the Act. • The Oversight Board may at any time issue such orders, rules, or regulations as it considers appropriate to carry out the provisions of the Act to the extent the issuance of such an order, rule or regulation is within the authority of the governor or the head of any department or agency of the government. Any such order, rule, or regulation is not subject to judicial review.
<p>209 – Oversight Periods Described</p>	<ul style="list-style-type: none"> • An "oversight period" is initiated upon the occurrence of any of the following events: failure of the government to provide sufficient revenue to a debt service reserve fund of the Oversight Board; the default by the government with respect to any loans, bonds, notes, or other form of borrowing; the failure of the government to meet its payroll for any pay period; the existence of a cash deficit of the government at the end of any quarter of the fiscal year in excess of the difference between the estimated revenues of the government and the estimated expenditures during the remainder of the fiscal year of the remainder of the fiscal year together with the first six months of the succeeding fiscal year; failure of the government to make required payments relating to pensions and benefits for current and former employees of the government; failure of the government to make required payments to any entity established under an interstate compact to which Puerto Rico is a signatory. • An oversight period terminates upon the certification by the Oversight Board that the government has adequate access to short- and long-term credit markets at reasonable interest rates, and for five consecutive fiscal years, the expenditures made by the government during each of the years did not exceed the revenues during those years. • An oversight period is deemed to exist upon the enactment of the Act.
<p>210 – Electronic Reporting</p>	<ul style="list-style-type: none"> • The Oversight Board chief financial officer may, in consultation with the Department of Treasury of Puerto Rico, ensure the prompt and efficient payment and administration of value added taxes and sales taxes including through the adoption of electronic reporting, payment and auditing reporting.
<p>211 – Oversight Board to Issue Bonds</p>	<ul style="list-style-type: none"> • The Oversight Board may at the request of the governor pursuant to an Act of the legislature issue bonds, notes, or other obligations to borrow funds in the name of and for the use of the government. The same is applicable at the request of the head of an agency or instrumentality with the authority to issue bonds, notes or obligations. • Any funds obtained through the issuance of bonds, notes or other obligations may be used for any purpose that the Oversight Board considers appropriate.
<p>212 – Pledge of Security Interest in Revenues of Puerto Rico</p>	<ul style="list-style-type: none"> • The Oversight Board may pledge or grant a security interest in revenues to individuals or entities purchasing bonds, notes, or other obligations issued. • The Oversight Board shall require the governor to pledge or direct taxes or other revenues otherwise payable to the government, including payments from the federal government, to the Oversight Board and to also transfer the proceeds of any tax levied for purposes of securing bonds, notes or other obligations.

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Comparison of PROMESA and H.R. 4900 (continued)

213 – Establishment of Debt Service Fund	<ul style="list-style-type: none"> As a condition to the issuance of bonds, notes, or other obligations, the Oversight Board shall establish a debt reserve fund. The debt reserve fund shall consist of such funds as the Oversight Board may make available and shall be a trust fund held for the benefit and security of all obliges of the Oversight Board. The funds may be used solely for the payment of the principal of bonds secured in whole or in part by such fund, the purchase or redemption of such bonds, the payment of interest of such bonds, or the payment of any redemption premium required to be paid. The Oversight Board may transfer any income or interest earned by or increments to any debt service reserve fund as it deems appropriate.
214 – Other Requirements for Issuance of Bonds	<ul style="list-style-type: none"> The Oversight Board may not issue bonds, notes or obligations that are secured in whole or in part by a debt service reserve fund if issuance of such bonds would cause the amount in the debt service reserve fund to fall below the minimum reserve requirement for such fund.
215 – No Full Faith and Credit	<ul style="list-style-type: none"> The full faith and credit of the U.S. is not pledged for the payment of any principal of or interest on any bond, note or other obligation issued by the Oversight Board.
216 – Duties of Oversight Board during Year Other than Oversight Year	<ul style="list-style-type: none"> Upon the termination of an oversight period, the Oversight Board shall, among others: review the budget of the government adopted by the legislature for each fiscal year occurring during such period; at any such time prior to the enactment of such budget as the Oversight Board considers appropriate, prepare a report analyzing budget and submit the report to the governor, the legislature, the President and Congress; and monitor the financial status of the government and submit reports to the governor, the legislature, the President and Congress if the board determines there is a risk that an oversight period may be initiated.
222 – General Assistance in Achieving Financial Stability and Management Efficiency	<ul style="list-style-type: none"> The Oversight Board may undertake cooperative efforts to assist the government in achieving financial stability, including assisting the government in avoiding defaults, eliminating and liquidating deficits, maintaining sound budgetary practices and avoiding interruptions in the delivery of services; and in improving the delivery of municipal services, the training and effectiveness of personnel of the government, and the efficiency of management and supervision.
233- Obtaining Reports	<ul style="list-style-type: none"> The Oversight Board may require the governor, the legislature, and the inspector general to prepare and submit such reports as it considers appropriate to assist it in carrying out its responsibilities under the Act.
224 – Reports and Comments	<ul style="list-style-type: none"> No later than 30 days after the last day of each fiscal year that is an oversight year, the Oversight Board shall submit a report to Congress describing, among others, the progress made by the government in meeting the objectives of the Act; the assistance provided by the Oversight Board; and any other activities of the board during the fiscal year. The governor shall submit any report submitted by him/her to the Oversight Board. The board will submit a report to Congress analyzing the completeness and accuracy of such reports. At any time during an oversight year, the Oversight Board may submit a report to Congress describing any action taken by the government of Puerto Rico that the board determines will adversely affect the government's ability to comply with an approved financial plan and budget. Unless the report contains confidential material, the reports shall be available to the public.
Title III - Sets Forth the Adjustments of Debts	
302 – Who May Be a Debtor <i>302 – Who May Be a Debtor</i>	<ul style="list-style-type: none"> Puerto Rico entities are considered debtors if <ul style="list-style-type: none"> A territory that is subject to an Oversight Board pursuant to an Act of the U.S Congress, or A territorial instrumentality of a territory; The Oversight Board on behalf of the entity has released the entity's audited financials for the most recently completed fiscal year; The entity is insolvent; The entity has completed negotiations to attempt voluntary debt restructuring; and The Oversight Board has authorized the filing of a petition. <i>Puerto Rico entities are considered debtors if</i> <ul style="list-style-type: none"> <i>A territory that has requested the establishment of an Oversight Board or has had an Oversight Board established for it by the U.S. Congress; or</i> <i>A covered territorial instrumentality of a territory;</i> <i>The Oversight Board has issued a restructuring certification under § 206(b) for such entity; and</i> <i>The entity desires to effect a plan to adjust its debts.</i> <i>Issuance of Restructuring Certificate:</i> <ul style="list-style-type: none"> <i>Puerto Rico completed process set forth in Title VI;</i> <i>The entity has adopted procedures necessary to deliver audited financial statements;</i> <i>The entity has adopted or is subject to a certified fiscal plan;</i> <i>The entity is insolvent;</i> <i>Appropriate consideration is given to relative priority of claims as established by law so that no one group or class of creditors gains an advantage that didn't exist prior to the Oversight Board's determination; and</i> <i>At least five of the seven members of the Oversight Board approve.</i>
304 – Petition and Proceedings Relating to Petition <i>304 – Petition and Proceedings Relating to Petition</i>	<ul style="list-style-type: none"> A case under this title may be commenced by the Oversight Board by filing a petition in the district court in which venue is proper. If the Oversight Board is filing petitions for more than one debtor, the Oversight Board shall file a separate petition for each debtor. <i>A voluntary case under this title is commenced by the filing with the district court of a petition by the Oversight Board, provided that an otherwise eligible entity may not commence a case under this chapter after the Oversight Board applicable to such eligible entity has been terminated.</i>
305 and 307 – Jurisdiction and Venue	<ul style="list-style-type: none"> District courts of the territory and the territorial instrumentalities. If the Oversight Board determines that such venue is inadequate, then the proper venue shall be in the district court of the jurisdiction where the Oversight Board maintains an office located outside the territory. <i>(Provision is numbers 306 and 307 in the H.R. 4900 version.)</i>
308 – Applicable Rules of Procedure	<ul style="list-style-type: none"> Federal Rules of Bankruptcy Procedure apply under this title. <i>(Provision is number 310 in the H.R. 4900 version.)</i>
309 – Role of Oversight Board	<ul style="list-style-type: none"> Oversight Board, for purposes of this title, serves as a representative of qualified debtors. Oversight Board is entitled to file a petition under § 304 or submit a plan of adjustment. <i>(Provision is number 315 in the H.R. 4900 version.)</i>
313 – Plan of Adjustment <i>312 – Plan of Adjustment</i>	<ul style="list-style-type: none"> Only the Oversight Board may file a plan of adjustment of debts. The Oversight Board may submit a joint plan of adjustment for multiple debtors if they are affiliates. <i>Only the Oversight Board may file a plan of adjustment of debts.</i>

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Comparison of PROMESA and H.R. 4900 (continued)

314 – Modification of Plan	<ul style="list-style-type: none"> • The Oversight Board may change the plan at any time before confirmation. <i>(Provision is number 313 in the H.R. 4900 version.)</i>
315 – Confirmation	<ul style="list-style-type: none"> • The court shall confirm the adjustment plan if: <ul style="list-style-type: none"> – Plan complies with the provisions of the Bankruptcy Code and this title; – Debtor is not prohibited by law to take any action necessary to carry out the plan; – Plan is in the best interest of creditors, – Plan is consistent with fiscal plan; and – Plan provides that all holders of administrative expense claims will receive, on effective date, cash equal to the amount of the allowed claim. <p><i>(Provision is number 314 in the H.R. 4900 version.)</i></p>
Title V – Sets Forth the Puerto Rico Infrastructure Revitalization Act	
502 – Revitalization Coordinator	<ul style="list-style-type: none"> • Establishes revitalization coordinator under the Oversight Board. Provides process for expediting the permitting process for “critical projects” consistent with Act 76. • Appointed by the governor within 10 days of receiving at least three nominations of possible candidates from the Oversight Board. • Qualifications: <ul style="list-style-type: none"> – Has not provided goods and/or services to government for the past three years; – Has not been an officer of the government for the past three years; and – Has substantial knowledge in planning/financing infrastructure projects. (Stronger consideration will be given to candidates with experience in energy projects).
503(a) – Critical Projects	<ul style="list-style-type: none"> • Any project sponsor may submit an existing, ongoing or proposed project to the revitalization coordinator and relevant Puerto Rico agencies. The application must include description of impact of project in society; immediate private funding access; economic benefits derived; current status of project; any other criteria requested by the revitalization coordinator, in consultation with governor; and if critical, project is energy project then detail oil dependence reduction, improve energy infrastructure performance, diversify energy source production and use energy sources from Puerto Rico.
503(b) – Critical Project Report	<ul style="list-style-type: none"> • Revitalization coordinator in consultation with relevant Puerto Rico agencies have 65 days (60 to complete and five to deliver) to prepare and deliver to the Oversight Board the critical project report containing: <ul style="list-style-type: none"> – An assessment of project meeting critical project criteria; – Governor’s recommendation; and – Revitalization Coordinator’s recommendations. • Oversight Board has 30 days to approve/disapprove critical project. If it fails to do so, the revitalization coordinator’s recommendation will prevail. <p><i>503(b) – Critical Project Report</i></p> <ul style="list-style-type: none"> • <i>Revitalization coordinator in consultation with relevant Puerto Rico agencies have 65 days (60 to complete and five to deliver) to prepare and deliver to the Oversight Board the critical project report containing:</i> <ul style="list-style-type: none"> – <i>An assessment of project meeting critical project criteria;</i> – <i>Governor’s recommendation;</i> – <i>Puerto Rico Energy Commission’s recommendation if an energy project is being considered; and</i> – <i>Revitalization coordinator’s recommendations.</i> • <i>Oversight Board has 30 days to approve/disapprove critical project. If it fails to do so, the revitalization coordinator’s recommendation will prevail.</i>
503(a)(3) – Certification of Expedited Permitting process	<ul style="list-style-type: none"> • Each Puerto Rico Agency has 20 days to submit their expedited permit process to the revitalization coordinator upon receiving a project submission. • If no expedited process is submitted within 10 days, the revitalization coordinator may develop an expedited permit process in consultation with the governor.
505 – Federal Agency Point of Contact Person	<ul style="list-style-type: none"> • Any federal agency with jurisdiction over Puerto Rico permitting, administrative or environmental review shall appoint within 30 days a point-of-contact person upon revitalization coordinator’s request. <p><i>505 – Federal Agency Point of Contact Person</i></p> <ul style="list-style-type: none"> • <i>Any federal agency with jurisdiction over Puerto Rico permitting, administrative or environmental review shall appoint within 30 days a point-of-contact person upon revitalization coordinator’s request.</i> • <i>Amended § 9 of the Consolidated and Further Continuing Appropriations Act, 2015:</i> <ul style="list-style-type: none"> – <i>Subsection (a)(5) – inserting “, except that, with respect to Puerto Rico, the term means, the Secretary of Energy” after “Secretary of the Interior”;</i> and – <i>Subsection (b) – inserting “(except in the case of Puerto Rico, in which case not later than 180 days after the date of enactment of the Puerto Rico Oversight, Management, and Economic Stability Act)” after “of this Act.”</i>
Title VI – Establishes the Process for Puerto Rico Debt Issuers to Submit Modifications on the Terms of the Bonds Issued by the Puerto Rico Government	
New Chapter. Not originally Included.	
601(a)(8) – Modification	<ul style="list-style-type: none"> • Means any modification, amendment, supplement or waiver affecting one or more series of bonds, including those effected by way of exchange, repurchase, conversion or substitution.
601(g) – Qualified Modification	<ul style="list-style-type: none"> • A modification will not be considered to be a qualifying modification unless — <ul style="list-style-type: none"> – The Issuer proposing the modification has consulted with holders of bonds in the pool for which the modification is being proposed prior to soliciting a vote on such modification; – Each participating bondholder is treated equally; – Outstanding principal of bonds is not reduced; – Bondholders retain secured liens; and – Modification is certified by the administrative supervisor as being consistent with fiscal plan and in the best interest of the creditors.
601(i) – Voting	<ul style="list-style-type: none"> • Qualifying modification may be proposed only by the issuer. • Affirmative vote or consent of holders of the right to vote the outstanding bonds of at least two-thirds of the aggregate outstanding principal amount of the outstanding bonds of all bonds in the pool.
J601(m) – Judicial Review	All causes of actions arising under this title will be reviewed by the U.S. District Court of Puerto Rico.

Feature

BY SONIA COLÓN AND JORGE L. SAN MIGUEL¹

Puerto Rico's Real Crisis Is Credibility

Editor's Note: For the latest news coverage on the island's financial crisis, visit ABI's "Puerto Rico in Distress" website at abi.org/PR-crisis.



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The Puerto Rico government's narrative over the past months — and that of some outsiders — has been narrow and seemingly convenient: Puerto Rico needs access to chapter 9 to address its debt crisis. The reasons stated include the island's economic contraction since 2006, its declining population due to migration, too large and nonpayable debt, and the fact that its government has cut costs severely and must continue to provide essential services, lest there be a more acute humanitarian crisis.

Unfortunately, this narrative is not sustained or justified by the available evidence and has led to local government inaction — beyond applying pressure on the federal government. It is also a myopic view that ignores the true and tested alternatives that Puerto Rico has readily available, regardless of federal action. Furthermore, it erroneously focuses on the symptoms instead of the root causes that led to the territory's current fiscal, economic and debt crisis.

Actions Speak Louder Than Words

The Puerto Rican government has been inconsistent in what it says and does. On Nov. 4, 2013, Gov. García Padilla stated that Puerto Rico had no liquidity problem, the public debt was payable, the Puerto Rico Constitution prohibits default and the government was not requesting aid from Congress.² On June 22, 2014, the governor indicated that his administration approved the territory's first balanced budget in 22 years.³ On June 28, 2015, however, the governor backtracked and announced that the \$72 billion in public debt was not payable.⁴

Transparency, Redefined

Transparency is also lacking. Puerto Rico has always had a history of disclosing public financial data. Until fiscal year 2012-13, the government had published audited *Comprehensive Annual Financial Reports* uninterrupted. Since then, however, for fiscal years 2013-14 and 2014-15, however, the government has not published any such reports.⁵

The current administration has not provided the general public, nor the investor community, with the minimum required financial information regarding the government's public finances and debt. The limited reports that have been produced are laden with qualifiers and disclaimers⁶ worthy of sound legal strategies, but that are poor and unacceptable for sound policy-making. Any discussions or request for public information by creditors with the island's Government Development Bank (GDB) or any of the government-controlled public corporations is subject to nondisclosure agreements and channeled through outside restructuring consultants.

Expense Cuts Have Been Legislated, but Not Realized

The local government legislated "cuts" in public expenses in 2014.⁷ The government claims to have cut costs severely and that it would be unable to make further reductions. Yet, an analysis from the Puerto Rico Office of Management and Budget revealed that one year following the enactment of this legislation, a total of 31 government agencies increased their trust positions payroll, while another 27 dependencies did not comply with the reductions in purchases of goods and services.⁸ During FY 2015 (2014-15), Puerto Rico spent more than \$13 billion through its Government Services Administration (GSA) in the procurement of goods and services for the government. This includes 39,000 contracts at the central-government level and 75,000 contracts at the municipal level (78 municipalities).⁹ Interestingly, the Puerto Rico legislature had enacted a law in 2011 intended to reach efficiencies at the GSA, but that law has not been implemented.¹⁰

International Experts Now Call for Pro-Growth Policies to Foster Needed Economic Growth

Recent economic reports ("Puerto Rico a Way Forward" and "Puerto Rico Recovery Plan") call for

¹ The authors offer special thanks to Francisco Pérez, a law clerk with Ferraiuoli, LLC, who contributed to this article. The opinions expressed herein are solely those of the authors and do not represent the opinion of Ferraiuoli LLC and/or any of the firm's clients.

² "Puerto Rico Has No Liquidity Problem, Governor Says," *Bloomberg Business*, Nov. 4, 2013.

³ "Puerto Rico Improving Under My Watch: Governor," *Bloomberg Business*, June 22, 2014.

⁴ Michael Corkery and Mary Williams Walsh, "Puerto Rico's Governor Says Island's Debts Are 'Not Payable,'" *New York Times*, June 28, 2015.

⁵ See Gov't Dev. Bank, available at bgfpr.com/investors_resources/commonwealth-cafr.html (unless otherwise specified, all links in this article were last visited on March 29, 2016).

⁶ See, e.g., Anne Krueger, Ranjit Teja and Andrew Wolfe, "Puerto Rico A Way Forward," June 29, 2015, available at bgfpr.com/documents/PuertoRicoAWayForward.pdf. See also, e.g., Puerto Rico Recovery Plan Report, Jan. 18, 2016, available at www.gdb-pur.com/documents/PRFEGPUpdatePresentation1.18.16-2.pdf.

⁷ P.R. Act No. 66 of June 17, 2014 (Act 66-2014), known as the "Government of the Commonwealth of Puerto Rico Special Fiscal and Operational Sustainability Act," calls for cuts in expenditures for goods and services and reductions in payroll expenses for employees in trust positions, among other things.

⁸ This constitutes a violation of Act 66-2014 and impeded the government from achieving greater cost reductions in at least \$91.1 million in operational expenses in 2015; see Limarys Suarez Torres, "Multiple Agencies Fail to Comply with Cuts," *El Nuevo Día*, Sept. 4, 2015, available at elnuevodia.com/noticias/politica/nota/multiplesagenciasincumplen-conlosrecortes-2095250.

⁹ The GSA runs auction processes and is responsible for the procurement of goods and services for the executive branch of the government, as well as municipalities and public corporations, yet many procurement processes are dispersed, segregated and managed at various levels of government (state, municipal, public corporations, judicial and legislative).

¹⁰ The GSA reorganization plan was legislated on Nov. 21, 2011, but has not yet been implemented.

economic growth as an essential ingredient to address the debt issue. Further, these reports state that no economic growth is possible without addressing structural obstacles. Ironically, beginning in 2009, Puerto Rico had embarked successfully — as evidenced by the Index of Economic Activity (IEA) issued by the Puerto Rico GDB¹¹ — in pro-growth economic policies. During that time period, Puerto Rico implemented tax reform¹² and permit reform,¹³ legislated a world-leading public-private partnership (P3)¹⁴ act,¹⁵ reduced government expenses, and paid its suppliers, among other things. It closed its first P3 transaction (PR Highways 22 and 5), which yielded a \$1.2 billion cash payment at closing and a \$600 million CAPEX commitment over 40 years — allowing for reductions in public debt and the transfer of operation and maintenance costs to a private operator for decades to come.¹⁶

Likewise, the San Juan International Airport successfully entered into a P3 agreement, yielding \$615 million at closing, a total of \$552 million in annual payments during the contract period, a CAPEX commitment of \$1.4 billion, and the transfer of long-term operation and maintenance costs and responsibilities to a world-class private operator.¹⁷ Puerto Rico's world ranking on government efficiency gained from 88/140 to 38/140 between 2009 and 2012.¹⁸ There was a growing sense of cautious optimism, and the discussion focused on how to continue growing and meeting the island's commitments.

Following the elections of November 2012, with a newly elected government, Fitch Ratings issued a press release on Dec. 18, 2012, warning the new administration to continue implementing policy decisions set forth by the outgoing administration.¹⁹ However, the mentioned pro-growth policies were reverted beginning in 2013, and the consequences became evident soon thereafter. For example, Act 40-2013²⁰ and Act 77-2014²¹ increased taxes and tax brackets. Act 151-2013²² reversed most of the permit reform established in 2009. The government increased its operating budget, did not undertake any P3 transactions, and stopped paying government suppliers.²³

As a consequence, Puerto Rico's multiple credits have been suffering nonstop credit downgrades from all three credit agencies.²⁴ Moreover, international competitive stud-

ies done by the World Bank Group and the World Economic Forum demonstrate the deterioration on Puerto Rico's classification in all major competitive ranges. Puerto Rico's ease of doing business classification by the World Bank Group went from 41/189 in 2014 to 57/187 in 2016.²⁵ Similarly, Puerto Rico's government efficiency classification descended from 38/148 in 2014 to 58/144 in 2015.²⁶ Now the island faces a large debt load, a stifling governmental structure,²⁷ and a heavily burdened and shrinking private sector, all of which has accelerated a worrisome migration trend.

Bankruptcy: No Solution

The U.S. Congress has held a total of nine congressional hearings to discuss Puerto Rico's challenges, including its energy infrastructure crisis and its fiscal and economic challenges, and whether and how access to chapter 9 of the Bankruptcy Code could be material in helping fix the island's ailments. Among the findings are that it is evident that Puerto Rico faces a difficult crisis, but its true scope and depth is not clear, since Puerto Rico suffers from significant and ongoing transparency issues.²⁸ Further, such hearings have demonstrated the inaccuracies of certain government-sponsored reports,²⁹ as well as the limitations of any chapter 9 or similar relief.

One point is eminently clear: Chapter 9 or similar bankruptcy relief is but a tool, rather than a solution. Puerto Rico's debt is not the problem, but a symptom resulting from its fiscal and economic policies. Furthermore, under chapter 9, most of Puerto Rico's challenges would remain untouched and unsolved, thus kicking the can on necessary reforms that, to the detriment of its 3.4 million residents, cannot wait. Chapter 9 will not deliver the benefits that are needed as the majority of the debt will not qualify, it will cause unnecessary and expensive litigation, and it will delay the inevitable fiscal and economic restructuring that now seems to have a consensus of support. In *Chapter 9 Municipal Bankruptcy: Utilization, Avoidance and Impact*, Michael De Angelis and Xiaowei Tian concluded:

If the primary objective of a financial distress mechanism is to provide a process to develop a solution to the financial difficulties of a municipality that can be sustained over time, the effectiveness of a Chapter 9 may depend on the underlying causes of the financial distress.... Without addressing the cities' core problems, the Chapter 9 process seems to have little impact on reversing the structural fiscal decline

11 As a result of these multiple pro-growth fiscal and economic initiatives, the GDB's IEA began an upward trend in December 2009 and broke into positive territory (for the first time since 2006) by November 2011-12. During that time, Puerto Rico received its best credit rating in recent history. S&P increased Puerto Rico's General Obligation credit rating from -BBB to BBB. See "Historical Credit Ratings," Gov't Dev. Bank, available at www.gdb-pur.com/investors_resources/documents/Sep2015-SPSHistoricalRatings-Eng.pdf; see also "Economic Activity Index," Gov't Dev. Bank (December 2015), available at www.gdb-pur.com/documents/2015-Dec-GDB-EAI.pdf.

12 P.R. Act No. 20 of Jan. 17, 2012, as amended.

13 P.R. Act No. 161 of Dec. 1, 2009, as amended.

14 P.R. Act No. 29 of July 8, 2009, as amended.

15 Statement of Motives of P.R. Act No. 237 of Dec. 19, 2014.

16 See Public Private P'ship Authority Transition Report at 14, available at www.transicion.pr.gov/2012/667/Informe%20status%20planes%20unidades%20administrativas/INFORME%20DE%20TRANSICION-Situaci%C3%B3n%20Actual%20de%20las%20Unidades%20Administrativas.pdf (the authors note that this document is written in Spanish).

17 *Id.* at 19.

18 Global Competitiveness Report 2015-16, World Econ. Forum, available at reports.weforum.org/global-competitiveness-report-2015-2016.

19 "Maintenance of Puerto Rico's Rating Will Depend on Policy Decisions," Reuters, Dec. 18, 2012. "The Commonwealth of Puerto Rico's general obligation bonds reflects the significant progress made by the outgoing administration in implementing widespread reforms despite economic underperformance. Maintenance of the rating will require policy decisions that continue this progress and achieve budget balance and a slowing in the growth of long-term liabilities..." *Id.*

20 P.R. Act No. 40 of June 30, 2013.

21 P.R. Act No. 77 of July 1, 2014.

22 P.R. Act No. 151 of Dec. 10, 2013.

23 Laura M. Quintero, "Supplier Debt Increases," *El Vocero* (Jan. 27, 2015), available at elvocero.com/engorda-la-deuda-con-suplidores. Ileanix Vera Rosado, "Bleeding Dry the Suppliers," *El Vocero* (April 10, 2016), available at elvocero.com/desangrados-los-suplidores-del-ela; Gerardo E. Alvarado, "\$2,098 Million Debt with Suppliers," *El Nuevo Dia* (April 2, 2016), available at elnuevodia.com/noticias/locales/nota/despidosyajustesporladeuda-2181838.

24 See Historical Credit Ratings, Gov't Dev. Bank, n.11.

25 "Doing Business Report 2016," World Bank Grp., available at doingbusiness.org.

26 World Economic Forum Global Competitive Report 2014-15, available at www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2014-15.pdf; World Economic Forum Global Competitive Report 2015-16, available at www3.weforum.org/docs/gcr/2015-2016/Global_Competitiveness_Report_2015-2016.pdf.

27 Puerto Rico has 3.4 million residents, 78 municipalities (each with one mayor) and 130 government agencies; by contrast, the City of New York has 8 million residents, one municipality, one mayor and 129 government agencies. New York City Agency Directory (March 23, 2016), available at www1.nyc.gov/nyc-resources/agencies.page; see also Citizen Budget Comm'n, NYC Debt Outstanding (March 22, 2015), available at cbcn.org/new-york-city-debt-outstanding.

28 U.S. Sen. Orrin Hatch (R-Utah) stated during the Finance Committee hearing held on Sept. 29, 2015, that "there is a lack of reliable data indicating what Puerto Rico has to show in return in terms of infrastructure, efficiencies, and improved economic performance." "Fin. & Econ. Challenges in Puerto Rico," Hearing Before Senate Committee on Fin., 114th Cong. (Sept. 29, 2015) (statement of Sen. Hatch, Fin. Comm. Chairman).

29 See, e.g., "Puerto Rico: The Krueger Fallacies," Dec. 14, 2015, by Carlos A. Colon de Armas, Finance Professor, Graduate School of Business, University of Puerto Rico.

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without debtors undertaking sustained fiscal consolidation. Many of the potential remedies for systemic fiscal distress relate to the political and governmental management of municipalities that a court in Chapter 9 procedures is restricted from interfering with.³⁰

Given the fiscal and the structural problems that Puerto Rico faces, the benefits of chapter 9 or similar relief are highly questionable.

A True Path Forward

Today, Puerto Rico does not have the luxury of time. It must tackle its fiscal, economic and debt structures — all at the same time. It must begin with re-establishing transparency and credibility with the general public, the capital markets and Washington, D.C. Strict internal controls and clear and effective reforms need to be properly *implemented and maintained* to guarantee transparency and encourage confidence from creditors and federal policymakers, as well as to agree to, or help foster, consensual negotiations and related agreements. Also, the government needs to cut spending intelligently. Any federal support, in the way of a federal oversight or control board, would ideally take all these components into consideration and support their respective restructuring.

Briefly, Puerto Rico can immediately implement four initiatives that do not require legislation, restructuring or chapter 9 or political risk, while having an aggregate value between \$5 billion to \$10 billion in annual revenue, cost-savings and economic investment in the short term:

1. *Improve tax collections, which have been historically low (56 percent vs. average mainland rate of 83 percent).* Improvement to a 65-70 percent collection rate would provide \$400 million to \$600 million in additional annual revenues.

2. *Implement efficient permit reform.*³¹ Reform can be achieved through executive orders from the governor.

This mechanism helped significantly in the development of multiple renewable energy projects between 2009-11, resulting in \$1.2 billion in direct investments.³² There remain many public infrastructure emergencies to address, including sewage, bridges, ports and solid waste. Such permitting reform can conservatively unleash between \$2 billion and \$3 billion in new investment.

3. *Reactivate P3s.* Puerto Rico has readily available public assets that can enter into P3 alliances, including the Puerto Rico Electric Power Authority (e.g., LNG Supply and Infrastructure Project of the North and Power generation facilities), Puerto Rico Aqueduct and Sewer Authority; Public Buildings and Puerto Rico Industrial Development Company real estate; Puerto Rico Highway and Transportation Authority's non-tax operations; Ports Authority facilities (e.g., Roosevelt Roads Port and the Rafael Hernandez International Airport); and Public Insurance Corporations (e.g., State Insurance Fund). These P3 transactions can yield \$2 billion to \$4 billion in revenues, in addition to displaced CAPEX investment and operation and maintenance costs over the long term.

4. *Implement government procurement reform.* Existing 2011 legislation would ensure that these procurements are centralized, transparent and leveraged in volume, thus realizing significant efficiencies. A mere 10-20 percent efficiency would save between \$1.3 billion and \$2.6 billion per year, based on the most recent procurement data.

Proper implementation and execution of these four initiatives will result in more revenues without increasing taxes, less government expenses, upfront liquidity, and improvement in the quality of infrastructure and services provided.

This will evidence traction, credibility and commence the path to sustainable recovery. Implementing practical and proven solutions will always trump policies that, by design or default, delay or avoid government decisions that otherwise benefit the people that it is supposed to serve. [cbi](#)

³⁰ Michael De Angelis and Xiaowei Tian, "U.S.: Chapter 9 Mun. Bankr. — Utilization, Avoidance and Impact," *Until Debt Do As Apart: Subnational Debt, Insolvency & Markets*, 311, at 334-35 (World Bank 2013).

³¹ Projects that create the greatest number of jobs (both direct and indirect) and most benefit the economy are those projects for which it takes it longest to obtain building permits (from the site consultation stage to the use permit stage) under the present system: (1) tourism projects take an average of 7.8 years; (2) commercial projects average 5.3 years; (3) affordable housing developments average 5.2 years; (4) private housing developments take 5.1 years; and (5) industrial projects average 3.3 years. *See* Statement of Motives of P.R. Act 161 (2009).

³² In 2010, the governor issued executive order No. OE-2010-034 of July 19, 2010, declaring a state of emergency in connection with the infrastructure of the Puerto Rico Electric Power Authority, the island's sole electric power utility. Unexplainably, the new administration terminated the designated emergency in May 2013 and with it, the expedited permitting process. *See* Executive Order No. OE-2013-038 of May 14, 2013.