

Committee on Natural Resources

Rob Bishop, Chairman

Hearing Memorandum

February 22, 2016

To: All Natural Resources Committee Members

From: Majority Staff, Committee on Natural Resources x5-2761

Hearing: Oversight hearing on “*The U.S. Department of the Treasury’s Analysis of the Situation in Puerto Rico*”

The Committee on Natural Resources will hold an oversight hearing on **Thursday, February 25, 2016 at 10:00 a.m. in room 1324 Longworth** entitled “*The U.S. Department of the Treasury’s Analysis of the Situation in Puerto Rico.*” This hearing will feature a discussion on the Obama Administration’s plan to address the Puerto Rican debt crisis.

Policy Overview

- The Committee’s two previous hearings in recent weeks on the Puerto Rican fiscal crisis have revealed there exists: 1) a desire to privately invest in Puerto Rico, 2) the potential for Puerto Rico to reach voluntary restructuring agreements with various creditors, and 3) a need for a strong, independent oversight body to ensure necessary reforms occur in Puerto Rico.
- The Administration’s plan to address Puerto Rico’s fiscal crisis involves four pillars: 1) access to debt restructuring, 2) implementation of strong independent oversight, 3) “adequate” treatment for Medicaid benefits, and 4) promotion of economic measures aimed at growth.
- Much of the debt restructuring proposed by the Administration may occur through consensual agreements between the creditors and Puerto Rico, if a strong, independent oversight authority exists to advocate for the development of such voluntary agreements.

Invited Witness

Mr. Antonio Weiss
Counselor to the Secretary
U.S. Department of the Treasury
Washington, D.C.

Background

The Commonwealth of Puerto Rico is in the midst of an economic and fiscal crisis, facing more than a \$70 billion debt,¹ and already defaulting on payments in the amount of \$174 million.² In turn, Puerto Rico may be on the cusp of a humanitarian dilemma – as it is forced to choose between providing public services, delivering pension benefits, or paying its debt. These critical issues have become a focal point for the Committee on Natural Resources (“Committee”), which has held two subcommittee oversight hearings over the past several weeks addressing different facets of the fiscal situation in Puerto Rico.

The first hearing, “*Exploring Energy Challenges and Opportunities Facing Puerto Rico*,” discussed the dire energy situation faced by the businesses and citizens of Puerto Rico due to the mismanagement of the electric utility, the Puerto Rico Electric Power Authority (PREPA). The hearing revealed the need for increased private investment on the island, and the potential for Puerto Rico to reach voluntary restructuring agreements with various creditors.

The second hearing titled “*The Need for the Establishment of a Puerto Rico Financial Stability and Economic Growth Authority*,” examined what an independent, federal oversight body would look like and what controls would be necessary to ensure future viability of Puerto Rico’s economy. Specifically, witnesses testified about the need for the oversight body to be of similar strength to the entity Congress crafted to oversee the District of Columbia’s financial problems in the 1990s.

Both hearings, and their associated witnesses, have resulted in calls to the Committee on the need for a legislative solution to the Puerto Rican fiscal situation, and what must be included in such legislation. Echoing these calls, the Administration through the U.S. Department of the Treasury (Treasury) has forwarded to Congress a legislative plan to address the debt crisis.

Treasury’s plan involves four “interrelated elements” that the Administration believes are necessary to address “Puerto Rico’s fiscal crisis and restore economic growth.”³ The four are summarized as follows: 1) access to debt restructuring, 2) implementation of strong independent oversight to improve Puerto Rico’s fiscal governance, 3) “adequate” treatment to Medicaid benefits, and 4) promotion of economic measures aimed at promoting growth.

¹ This total excludes unfunded amounts owed, such as the ERS, TRS, and JRS pensions, which combined total an additional \$40 billion.

² Mary Walsh, “Puerto Rico Defaults on Debt Payments”, Jan. 4, 2016 available at <http://www.nytimes.com/2016/01/05/business/dealbook/puerto-rico-defaults-on-debt-payments.html? r=0>.

³ Hearing on Puerto Rico: Economy, Debt, and Options for Congress, Before the S. Comm. On Energy and Natural Resources, 114th Congress (Oct. 22, 2015) (written testimony of Antonio Weiss, Counselor to the Secretary, U.S. Department of the Treasury).

Debt Restructuring

Mr. Weiss, in prior testimony before the Senate Committee on Energy and Natural Resources, stated “a central element of any Congressional response must include a fair and orderly restructuring mechanism built on the tested principles of the federal bankruptcy code.”⁴ The underlying premise to Treasury’s position is the perceived unsustainability of “Puerto Rico’s debt load.”⁵ Thus, the Administration proposes that such mechanism should provide for a “comprehensive restructuring of all of Puerto Rico’s outstanding debt,”⁶ including the debt guaranteed by Puerto Rico’s Constitution.⁷

Opponents of the Administration’s proposal assert blanket restructuring authority “could have a damaging effect on the U.S. municipal bond market” and “make it extremely hard for Puerto Rico to return to the capital markets after the current financial storm eventually passes.”⁸ Essentially, skeptics argue that by undermining Puerto Rico’s constitutionally guaranteed bonds, any such guaranteed bond in the future – even those issued by states – will be met with skepticism.

However, Puerto Rico’s current constitutionally guaranteed debt obligation far exceeds the limits for such obligations that are written into the same guaranteeing clause of the Puerto Rican Constitution.⁹ As such, Puerto Rico has been undermining the credibility of its own constitutionally guaranteed debt for decades.

A further possible solution would be to promote voluntary agreements between creditors and Puerto Rican debtors. Exemplifying this notion is the restructuring agreement reached between PREPA and 70% of its bondholders. This agreement provided PREPA with five-year debt service relief of over \$700 million, a principal debt reduction of more than \$600 million, and a refund to PREPA of \$115 million of the January 1, 2016 interest payment.¹⁰ Consensual agreements such as this could obviate the need for forced debt restructuring and provide viable paths forward for much of Puerto Rico’s debt.

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ See P.R. Const. art. VI, § 2.

⁸ Arturo C. Porzecanski, Congress Shouldn’t Provide a ‘Super Chapter 9’ Escape for Puerto Rico, Nov. 6, 2015, available at <http://www.forbes.com/sites/realspin/2015/11/06/congress-shouldnt-provide-a-super-chapter-9-escape-for-puerto-rico/#5e24823c5cb9>.

⁹ See P.R. Const. art. VI, § 2.

¹⁰ PREPA, PREPA Agrees to Financial Restructuring Plan with Major Financial Creditors, Dec. 24, 2015, available at http://www.aeepr.com/Docs/PREPA_RSA.pdf.

Independent Fiscal Oversight

The second component of the Administration's plan to address the Puerto Rican fiscal crisis is the implementation of "strong fiscal governance and oversight."¹¹ Such oversight "should provide sufficient safeguards to ensure Puerto Rico adheres to its recovery plan and fully implements proposed reforms."¹² However, the Administration's plan constrains the authority of such independent oversight by requesting it respect "Puerto Rico's autonomy."¹³

At the Senate hearing last fall, Mr. Weiss acknowledged that Puerto Rico's efforts to address its fiscal crisis "have been hampered by a lack of fiscal oversight and transparency."¹⁴ Consequently, Puerto Rico has "relied on unrealistic revenue estimates" as "proposed revenue and expense measures have fallen short because Puerto Rico lacks important fiscal controls to ensure discipline."¹⁵ Indeed, the failure for Puerto Rico to provide audited financial statements for the past two fiscal years exemplifies the systemic problems within Puerto Rico's accounting and financial systems.¹⁶ Thus, such independent oversight must have the ability to effect change over Puerto Rico's finances.

With Puerto Rican legislators already vowing to "dam up" and hinder any independent authority that requires Puerto Rican ratification, it is unclear how deferential any such proposed oversight authority should be to Puerto Rico's autonomy.¹⁷ The Administration has failed to clearly define what "respecting Puerto Rico's autonomy" entails. However, as the former Chief Financial Officer to the District of Columbia's Financial Responsibility and Management Assistance Authority and former Mayor Anthony Williams, recognized, any such authority must be able to take the necessary steps to address the short, medium and long term issues to ensure the future viability and sustainability of Puerto Rico's economy.¹⁸

¹¹ The White House, Addressing Puerto Rico's Economic and Fiscal Crisis and Creating a Path to Recovery: Roadmap for Congressional Action ("Path to Recovery"), at 7, available at https://www.whitehouse.gov/sites/default/files/roadmap_for_congressional_action_puerto_rico_final.pdf.

¹² *Id.*

¹³ *Id.*

¹⁴ Hearing on Puerto Rico: Economy, Debt, and Options for Congress, Before the S. Comm. On Energy and Natural Resources, 114th Congress (Oct. 22, 2015) (written testimony of Antonio Weiss, Counselor to the Secretary, U.S. Department of the Treasury).

¹⁵ *Id.*

¹⁶ Michelle Kaske, Puerto Rico Fails to Provide Fiscal 2014 Report by Deadline, Oct. 31, 2015, available at <http://www.bloomberg.com/news/articles/2015-10-31/puerto-rico-fails-to-provide-fiscal-2014-report-by-deadline>.

¹⁷ El Nuevo Dia, Legislators Predict Clear Opposition to Federal Board, Feb. 18, 2016.

¹⁸ Mayor Anthony Williams, Remarks at the Bipartisan Policy Center on Puerto Rico's Debt Crisis: Strategies and Solutions (Feb. 5, 2016).

Medicaid Treatment and Economic Growth

The final two components of Treasury's plan both may be summarized as expanding access to federal benefits. The first, Medicaid treatment, is highlighted by Treasury due to the Administration's conclusion that "the 3.5 million Americans in Puerto Rico are left without access to healthcare treatments considered standard in the rest of the nation."¹⁹ The component concerning economic growth hinges on providing Puerto Rico access to the Earned Income Tax Credit ("EITC"). Both of these proposed programs would require substantial increased financial involvement by the federal government.

Treasury indicates that there are more than 1.6 million Medicaid enrollees in Puerto Rico, which accounts for 45% of the population. Nationally, only 22% of the population receives Medicaid benefits.²⁰ However, when further compared, Puerto Ricans receive \$1,571 per enrollee, whereas the average recipient in the U.S. receives \$5,790.²¹ Furthermore, Treasury believes 600,000 recipients will lose access to Medicaid once an additional \$5.4 billion in funding that was provided by Section 2005 of the 2010 Patient Protection and Affordable Care Act (PPACA) expires in 2019.

¹⁹ Path to Recovery, *supra* note 11, at 8.

²⁰ See State Medicaid & CHIP Profiles, available at <https://www.medicaid.gov/medicaid-chip-program-information/by-state/by-state.html>.

²¹ Maria Levis, The Price of Inequality for Puerto Rico, Dec. 29, 2015, available at <http://healthaffairs.org/blog/2015/12/29/the-price-of-inequality-for-puerto-rico/>.