

Committee on Natural Resources
Oversight Hearing
1324 Longworth House Office Building
Thursday, May 9, 2019
10:00 am

Hearing on “*The Status of the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA): Lesson Learned Three Years Later.*”

Questions from Chairman Grijalva for Hon. Ricardo A. Rosselló, Governor of Puerto Rico

1. Section 2141 (b)(1)(B) of PROMESA requires that Fiscal Plans approved by the Fiscal Oversight and Management Board (FOMB) for Puerto Rico “ensure the funding of essential public services.” In your testimony, you mentioned that you and your Administration have not formally defined the term.

How do you define “essential public services”? What framework and targets has your Administration implemented to ensure that “essential public services” are available to the residents of Puerto Rico? Also, do you consider PROMESA should be amended to include a more specific definition of “essential public services”?

2. How are the PROMESA Fiscal Plans developed? Does the FOMB write them and send them to you for your approval or is it a collaborative effort?

Other than opposing the various labor reforms that the FOMB proposed, has your administration been supportive or opposed to the cuts to education, the University of Puerto Rico and health care? Have you proposed budgets to restore those cuts that were rejected by the FOMB?

3. The Middle States Commission on Higher Education has placed the University of Puerto Rico (UPR) in show-cause status due to its fiscal situation and financial projections. The UPR is at risk of losing its accreditation and access to federal funds.

Has your Administration engaged and collaborated with other stakeholders, such as the University Board, to develop the UPR’s budget and Fiscal Plan? Please share information about the stakeholders that have participated in the process and the extent of their participation.

4. The agreement reached between PREPA and a good part of its creditors will cause an increase of up to 4.6 cents per kilowatt hour, which when added to other scheduled adjustments for the rate, would imply an increase of up to 30% in the cost energy in Puerto Rico in several years.

Has the Government considered how this will hurt workers in Puerto Rico who on average make less than \$20,000 per year, or slow down the creation of jobs by local businesses? Can local businesses and the people of Puerto Rico afford a 30% increase in energy cost? Wouldn't a rate increase hurt the ability of Puerto Rico's economy to recuperate?

5. The Trump Administration has expressed concerns regarding financial controls in Puerto Rico to justify reluctance to provide further funding for disaster relief and recovery for the island.

In terms of financial controls, what is the division of fiduciary responsibilities among the Governor's office, the Puerto Rico Fiscal Agency and Financial Advisory Authority, the Puerto Rico Comptroller, and the FOMB?

6. Section 208(b) of PROMESA requires a report on discretionary tax abatement agreements. Your Administration has avoided publicly disclosing the contents of the report. However, without this information it is difficult to track how much revenue Puerto Rico is losing from individually tailored corporate tax breaks.

Why has that information not been disclosed? Please provide an analysis of how much Puerto Rico benefits from these tax breaks versus how much controlled foreign corporations (CFCs) bring to the island's economy.

Questions from Chairman Grijalva for Ms. Natalie Jaresko, Executive Director, Financial Oversight and Management Board

1. Section 2141 (b)(1)(B) of PROMESA requires that Fiscal Plans approved by the FOMB "ensure the funding of essential public services." In your testimony, you mentioned that the FOMB has not defined the term. That is particularly worrisome, given that the FOMB has certified fiscal without defining any sort of funding baseline necessary to ensure essential public services.

What is the FOMB's definition of the essential public services that any government should guarantee to provide for the care and well-being of its citizens? Why is the FOMB promoting the approval of debt adjustment plans without defining those essential public services? How do the fiscal plans certified by the FOMB reflect a commitment to guaranteeing human rights and basic needs of residents of Puerto Rico? Also, do you oppose PROMESA being amended to include a more specific definition of "essential public services"?

2. Upon the departure of Mr. Noel Zamot, you assumed the role of Revitalization Coordinator for the Financial Oversight and Management Board (FOMB). What critical infrastructure projects is the FOMB considering?

3. Please provide a list of the FOMB's registered lobbying firms. Include the total authorized annual cost, the duration of the contract, and what each firm is lobbying for or against.
4. In your testimony, you mentioned that proposed budget cuts to the University of Puerto Rico would only result in a consolidation of "back-office functions". In addition, you mentioned that if certain administrative savings and a new focus on improving revenues are implemented, then no cuts to faculty or student services are necessary.

Has the FOMB or its consultants performed a study to assess the feasibility of consolidating back-office functions and reaching target administrative savings? Please share the results of the assessment.

5. The FOMB has challenged the legality of more than \$6 billion in General Obligation (GO) debt issued after 2012. Almost simultaneously, the FOMB declined to challenge the legal basis for the COFINA deal. What process and rationale did the Board follow to decide which debt issuances to challenge?
6. What specific measures, if any, has the FOMB implemented to identify and redress conflicts of interest in its decision-making, advising, and investigative processes?
7. Were FOMB members checked for personal and professional conflicts of interest at the time of their appointment and have these background checks been made public?
8. Section 104(o) of PROMESA establishes that "the Oversight Board may investigate the disclosure and selling practices in connection with the purchase of bonds issued by a covered territory for or on behalf of any retail investors including any underrepresentation of risk for such investors and any relationships or conflicts of interest maintained by such broker, dealer, or investment adviser as provided in applicable laws and regulations." In addition, Section 104(p) establishes that the "Oversight Board shall make public the findings of any investigation references in subsection (o)."

Why did the FOMB request to hide the identity of individuals, corporations, and institutions potentially responsible for issuing illegal debt as part of a list of possible defendants submitted to the U.S. District Court for Puerto Rico in April 2019?

9. The Government of Puerto Rico - at least the elected part vs. the federally-imposed part - appears to be matching the FOMB's spending on outside lawyers and financial consultants dollar for dollar, even though PROMESA provides for the FOMB to represent the territory on debt matters. Have you tried to work out joint hiring of lawyers, financial consultants, and others to save Puerto Rican taxpayers hundreds of millions a year?

10. Can you explain why the 2017 Fiscal Plan that was released before the hurricane called for large reductions in debt repayment – between 75 and 85 cents on the dollar -- while the current plan appears not to be as aggressive?
11. One of the FOMB's biggest and most consistent complaints about the Government of Puerto Rico is the Government not adopting what the Board terms "labor reforms." Chief among these is the Government not repealing the longstanding law that requires severance pay for employees fired without cause. The Chairman of the Board wrote an op-ed in the New York Post reiterating this complaint just this week.

Why did the FOMB repeatedly refer to an agreement with the Governor as an agreement with the Government? Doesn't it understand the separation of powers in a republican form of government?

Why didn't the FOMB negotiate a proposed change in law with the Legislative Assembly, which writes the laws?

12. How do the income and economic growth projections included in the certified Fiscal Plans compare with the actual reports on income generated by the Government of Puerto Rico? If the income and economic growth projections included in the certified Fiscal Plans are not met, does the FOMB have a Plan B to ensure funding for essential public services and compliance with debt adjustment plans?
13. The FOMB's certified Fiscal Plan for the territory as a whole would require the Government of Puerto Rico to spend \$1.162 billion of Puerto Rican tax dollars on Medicaid during the fiscal year that begins July 1st and \$2.294 billion in Fiscal Year 2021. Those would be increases from zero this territorial fiscal year and \$123 million in FY 2018. To spend the amount dictated by the FOMB, the Government of Puerto Rico will have to cut spending in other areas to generate these amounts for Medicaid.

Do you recognize that you have constructed a Fiscal Plan that insists its spending limits across the board are enough, so that increasing Federal funding for Medicaid in Puerto Rico would increase the budget surplus from which bond creditors could claim they should be?

14. The Puerto Rico Sales Tax Financing Corporation - "COFINA" - is an instrumentality of the Government of Puerto Rico. It was created a dozen years ago in response to a budget crisis solely to enable the territory to borrow more than permitted by its constitution. COFINA bonds of close to \$18 billion totaled a quarter of the territory's bonded debt and a third of the debt that the FOMB wants to adjust.

Another quarter and third of the debt are "General Obligation" or "GO" bonds issued or guaranteed by the Government of Puerto Rico itself. According to the territory's

constitution, payment on these bonds must be made before any other expenditure of the Government.

Section 201 (a) of PROMESA requires the FOMB to “respect the relative lawful priorities or lawful liens . . . in the constitution, other laws, or agreements” of Puerto Rico. The FOMB has asked the PROMESA bankruptcy court to void more than \$6 billion of the nearly \$18 billion in GO bonds because it exceeds the constitutional limit on borrowing.

The FOMB’s settlement with COFINA creditors is paying senior COFINA bond holders 94 cents of face value and junior COFINA holders 56 cents - with a 3.5% bonus for the big owners, with which it primarily worked out the deal. Among these are hedge funds that bought the bonds for far less than the amount that they will be paid under the deal. Many Puerto Rican credit unions, other institutions, and individuals, especially retirees own junior COFINAs. Some hedge fund speculators with which the FOMB worked out the COFINA deal are making profits of more than \$1 billion.

Why doesn’t the FOMB limit recoveries to what bond creditors paid for the debt?

Why did the FOMB work out a deal with COFINA creditors that allows windfall profits before working out a deal with GO bondholders?

Are you confident that the Puerto Rican economy will be able to sustain both the new COFINA bond payments and the payments that will need to be made on other bonds?

How does so much COFINA revenue going to bondholders affect the ability of the Government of Puerto Rico to make payments on the priority bonds issued or guaranteed by the territory?

15. Current piecemeal debt negotiations have neglected to look at Puerto Rico’s ability to sustainably repay all its debt. A Debt Sustainability Analysis authored by economist Martín Guzmán indicates: “the generosity with the COFINA bondholders can only be sustained if the reduction on the rest of the public debt lies between roughly 85% and 95%—a conclusion that rests on the assumption that the entire public debt restructuring is designed with the goal of restoring debt sustainability.”

Notwithstanding, in the hearing you expressed your goal of using approximately 10 percent of Puerto Rico’s own resources to debt service.

How do you suppose Puerto Rico could be left with a debt load comparable only with the richest states, such as that of Florida, which has a with a population of little over 21 million and own revenues of almost \$41 billion versus that of Puerto Rico, which has a population of roughly 3.2 million and general revenues of roughly \$10 billion? If you look at the whole picture, how much of the debt stock will be

reduced? How do you prevent the island from falling prey to a future default on its debt?

Questions from Chairman Grijalva for Mr. Martín Guzmán, Fiscal Policy Fellow, Espacios Abiertos

1. In your testimony, you mentioned that “delays in concluding debt restructurings make economic recessions deeper and longer.” What specific changes should the FOMB, the Government of Puerto Rico, and Congress implement in the short-term to ensure that Puerto Rico’s debt restructuring process is successful and does not result in a longer recession?
2. According to your testimony, the FOMB and the Government of Puerto Rico have overstated the savings of the COFINA deal and understated the risks of those debt negotiations. Can you further explain how your assessment of the COFINA deal differs from the assessment performed by the FOMB?
3. According to your calculations, the COFINA agreement can only be sustained if the reduction on the rest of the public debt is between 85% to 95%. Have other jurisdictions reached this type of debt restructuring agreement and is it practical to achieve it?
4. The 2018 Fiscal Plan certified by the FOMB required a Human Capital and Labor Reform that implements employment at-will and a reduction of mandated paid leave. Does research support the implementation of labor-market reforms to achieve economic development during a recession?
5. Are you aware of any other case of massive primary surpluses projected in the first 10 years of a debt restructuring deal, that is then followed by declining negative ones? If Puerto Rico’s economy continues to wither, what are the implications of the current debt restructuring deals down the line, say in about 15-20 years?

Questions from Chairman Grijalva for Ms. Amanda Rivera, Executive Director of The Institute for Youth Development

Section 2141 (b)(1)(B) of PROMESA requires that Fiscal Plans approved by the Fiscal Oversight and Management Board for Puerto Rico “ensure the funding of essential public services.”

6. Would defining “essential public services” help improve the quality of life of children in Puerto Rico? Please explain why or why not.

Questions from Chairman Grijalva for Ms. Ana C. Gómez-Pérez, Associate Professor at the University of Puerto Rico:

1. In your testimony, you stress that the University of Puerto Rico (UPR) has made important contributions to the economic development of the island. Has the UPR or an independent entity quantified the financial impact of these contributions? Please provide supporting documentation.
2. Has the UPR assessed the possibility of a reformed system of income- or means-based tuition? Please explain why and the status of the assessment.
3. The UPR annually graduates thousands of students – highly educated engineers, lawyers, bankers, and teachers. In your opinion, how can Puerto Rico best leverage the research and human capital of the UPR as an economic multiplier? What role can the UPR play to offset the amount being spent on outside consultants?