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Should Virginians Help Bail Out Puerto Rico?

By Michael Thompson

6/1/2015 -- Puerto Rico is in serious financial crisis, and because the island is a U.S. territory, this is a matter of concern to taxpayers in Virginia and throughout the country. As a territory, this government cannot declare bankruptcy under current Chapter 9 law, but it wants to do just that.

No government gets itself into this kind of trouble with its eyes closed. Today it owes some \$74 billion in current debts, with long term liabilities exceeding \$160 billion.

This summer major payments are due bondholders and it looks as if those payments may not be made. So what is the territorial government asking of Congress? They want authority to declare bankruptcy and leave hundreds of thousands of Americans, including many here in Virginia, holding worthless paper.

Decades of government overspending and unrealistic government pensions and health care have left the island with a staggering \$164 billion in short and long term debt. The island government and its non-voting member of Congress want the taxpayers to bail out Puerto Rico. That legislation is pending in the House Judiciary Committee, chaired by Virginia's highly respected Congressman Bob Goodlatte.

Bailout legislation would be a bad precedent, and leaves unaddressed Puerto Rico's current system of financial mismanagement.

Bonds were purchased by individuals and investment funds knowing that under the current law Puerto Rico cannot declare bankruptcy. That was a major reason that people felt comfortable buying bonds from this U.S. territory. To change that and allow bankruptcy would send all sorts of negative messages. For instance, with that precedent the federal government could, when the time comes, decide not to pay its own obligations for Social Security, US Treasury bonds, or other obligations. If it was good enough for Puerto Rico, then clearly it is good enough the United States.

As mentioned above, what happens in Puerto Rico matters to Virginians. To be sure, something needs to be done. But Chapter 9 bankruptcy protection is an ill-advised solution for Puerto Rico and a perilous precedent for the United States.

Bankruptcy would simply allow Puerto Rico's leaders to walk away from its debt with little repercussion for themselves. The net result would be U.S. taxpayers underwriting a bailout and U.S. seniors and working Americans being forced to absorb financial losses for problems not of their own making. This idea should be discarded by the House Judiciary Committee and Puerto Rico told to make the tough, restructuring decisions that the real world requires.

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Bankruptcy would negatively impact on the territory's current investors and court cases would be instituted that will end up costing the taxpayers even more money with the outcome possibly in doubt. No one knows how the courts would rule and then Congress might be right back in the middle. And the island would be an even worse economic basket case than it is today.

Allowing Puerto Rico to declare bankruptcy is not allowed under current law and the island knew that when it created an unsustainable financial network of government businesses and obligations. One example of the financial mismanagement is that over \$200 million in past due electric bills are due from government agencies to the government run electric utility. And this utility is the major debtor of the island government!

There are better options available.

Puerto Rico can negotiate with bondholders requiring it to make substantial changes in its financial management of the island's public businesses. There are indications this is going on today but the island territory is reluctant to make required changes hoping that Congress will bail it out. That is exactly why Congress should not.

And there is a time-tested action Congress can take that would make a lot more sense. In the 1990's Washington DC was in grave financial trouble and Congress created a Financial Control Board that took over the city's finances. A Financial Control Board can restructure the Puerto Rican government, consider selling its government businesses, and reform its tax code.

It is clear that Puerto Rico's political leaders are not up to the task of making the tough and perhaps unpopular choices needed to put the Island on a sound financial course. A Financial Control Board worked 20 years ago for the District of Columbia and our capital city is in much better financial shape today.

Virginians who invested in Puerto Rico through buying government bonds directly and through their retirement funds should not take the financial hit for gross mismanagement by this island territory. And, one of the requirements for any US government efforts to help Puerto Rico out of its current financial troubles should be that it will never become a state. Its financial mismanagement should disqualify it from ever reaching that status.