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### PROMESA, Puerto Rico's Recipe for Disaster

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# PROMESA, Puerto Rico's Recipe for Disaster

*The 2016 bankruptcy law has brought high costs, austerity measures, migration and a deeper economic recession for the U.S. territory.*

By: Cristina Corujo

Aliana Margarita Bigio is known for advocating online for a better life for all Puerto Ricans. Ever since she started to see how her day-to-day life was affected by the island's financial crisis, she has been using her Instagram account, ['ConSentimientoPR'](#), to speak up against what the local and federal governments are doing to the citizens of Puerto Rico.

"Puerto Rico wants justice," Bigio wrote on one of her last [social media posts](#) during last weeks protest on the island, while holding a banner that said 'Gobierno Asesino' (Killer Government.)

The 23-year-old student, a political science major at the University of Puerto Rico, enrolled in the Rio Piedras campus in San Juan in 2016, the same year President Barack Obama signed the Puerto Rico Oversight, Management and Economic Stability Act (PROMESA), designed to fix the island's financial crisis, which began more than a decade ago.

PROMESA was signed with the purpose of helping the island's economy recover from its crippling indebtedness. Instead, it has brought financial and social instability as costs related to the recovery climb to at least \$1 billion and a island-based Financial Oversight Management Board that has yet to identify the essential services required to keep the island's social and physical infrastructure intact.

PROMESA, which grants Puerto Rico the right to file for bankruptcy, became public law on June 30, 2016. Puerto Rico's status as a U.S. territory ordinarily disqualifies the island's government from declaring bankruptcy and restructuring. Nor can it get other financial help because of its colonial status. In effect another version of the U.S. bankruptcy law commonly called Chapter 9, PROMESA also protects Puerto Rico from bondholders' lawsuits as it struggles to recover. The law frees the mainland from responding to the financial crisis and installs an oversight board, which has imposed widespread austerity measures -- resulting in proposed cuts in everything from education to government pension payouts.

"Getting rid of the board is the same as saving Puerto Rico," said Bigio.

Since day one, the oversight board has faced criticism. And now it is facing harsh pushback, as well as legal challenges. The board's legality is currently before the U.S. Supreme Court, with opponents to its existence arguing that its 7 members, appointed by the President, were never confirmed by the U.S. Senate and it's still not clear if the members are board are considered to be federal officials.

The board's financial recommendations -- most of them cutbacks in local spending -- have been imposed as even more crises have hit Puerto Rico. Recently the island has been struggling with hundreds of earthquakes in the last two weeks, while still trying to recover from the 2017 hurricane that took more than 3,000 lives and caused more than \$100 billion in damage.

### **Monetary Cost:**

Under PROMESA, the cost of Puerto Rico's bankruptcy case is increasing rapidly as time passes. The latest, almost \$1 billion, includes \$250 million in legal fees billed to the territory from 2014 to 2016, before the law was passed and the oversight board arrived on the island.

Mostly focused on lobbying in favor of PROMESA, the law firms that have received these contracts include such major players as Proskauer Rose, Aliz Partners, Millstein & Co. and Cleary Gottlieb, according to [reports](#) in El Nuevo Día, the leading Puerto Rican daily.

Reports posted on the oversight board's website states that the board has spent a total of \$155 million on administrative and legal fees as of July 31, 2019. That will continue to rise.

Meanwhile, the Sales Tax Financing Corporation (COFINA), a bond fund created in 2007 to finance the island's government expenses, has paid \$332 million in fees to law firms and advisors working in the restructuring process.

Other bankruptcy-related agencies and organizations are adding even more fees. These include the Fiscal Agency and Financial Advisory Authority, a local committee formed to oversee financial stability on the island; the Unsecured Creditors Committee, composed by debtors who aren't secured; the Official Committee of Retirees (COR, in Spanish), made up of some government pensioners; and the bankruptcy's mediation team.

As of January 2019, the advisors, attorneys and others from these groups had earned \$205 million.

[//www.datawrapper.de/\\_/5P4N7/](http://www.datawrapper.de/_/5P4N7/)

“Bankruptcies are expensive,” said bond researcher Cate Long, who’s been following Puerto Rico’s case for years now.

When Detroit filed for Chapter 9 in 2013 for its \$18 billion debt, fees and expenses were calculated at \$178 million. But critics of the recovery costs in Puerto Rico, whose central government debt is estimated at more than \$72 billion, say much of the bankruptcy expense arises from overspending.

“Congress and the Judge Laura Taylor Swain have said there is an excess of expenses when it comes to consultants,” said economist Iyarí Ríos, who’s a professor at the University of Puerto Rico

Those providing these professional services are mainly law firms that have been hired to restructure debt itself and to litigate conflicts between the oversight board, the Puerto Rican government and bondholders. Already, conflicts between the local government and the board, have ended up in federal courts.

Economists say some of the conflicts stem from a lack of transparency from the administration of former Puerto Rican Governor Ricardo Rossello, who was forced to resign on July 24 after mass demonstrations called for his ouster following a leaked sexist and homophobic electronic chat between him, his staff and others. But some conflicts also arise, critics say, from a lack of transparency within the oversight board.

Rolando Emanuelli, a Puerto Rican lawyer and co-author of the book “PROMESA,” published in 2016, says the board’s failure to publicly account documents related to Puerto Rico’s restructuring process has contributed to its high fees. Litigation among the board, bondholder and the local government has increased the boards cost in payments to attorneys, advisors and others.

“We could have avoided all these costs,” he said.

A recent proposal from U.S. Representative Raúl Grijalva, a Democrat from Arizona’s Third Congressional District, recommends amending PROMESA to have a federal funding pay for all expenses instead of taking the money from the local government’s budget. But there are no clear signs that these proposed provisions will pass.

“If they are passed in the house, they will never be discussed by the Senate and it will never be signed by the president,” said Representative Rob Bishop, a Republican from Utah’s First

Congressional District, speaking at the House Natural Resources Committee Hearing in October 2019. Historically this committee has been the one working with everything related to Puerto Rico.

Meanwhile, expenses continue to rise. At last calculation, on October 2019, Puerto Rico's total bankruptcy costs were at \$942 million and there is still a long way to go.

The oversight board, for instance, hasn't been able to fulfill the two tasks required for its work to be over: creating a balanced local budget for four consecutive years and bringing Puerto Rico back to the debt market.

Emmanuelli and others following the recovery efforts were expecting 2020 to be the first year for the first balanced budget. But approval for the budget is in the hands of Laura Taylor Swain, the federal judge overseeing Puerto Rico's bankruptcy case, and she has yet to make a decision, given the strong objections on spending cuts that are publicly expressed throughout the island.

"Maybe 2021," said Emmanuelli.

### **Social Cost:**

Bigio, now a senior at the University of Puerto Rico, still remembers how difficult it was to find a campus parking space back in 2016, given the large number of students enrolled. But now, she says, the story is completely different. "Now we have a ton of free space," she said.

Since 2009, when the island's recession began, Puerto Rico has seen high numbers of migration. In the last decade, at least half a million people fled the island, looking for a better future.

Bigio and others say the austerity measures imposed by the oversight board will only intensify the migration crisis.

"We will have a Puerto Rico without Puerto Ricans," said Bigio, who's seen some of her classmates leave the island.

Although the exodus has been going on for years, once Hurricane María hit the U.S. territory more than two years ago, the pace of migration quickened, as essential services continue to worsen against a backdrop of continued cuts from the oversight board.

Education is one of the hardest-hit sectors. In the past two years, at least 25% of the island's elementary and high schools have closed. "It's the biggest we've seen," said economist Jose

Caraballo-Cueto, a prominent professor at the University of Puerto Rico and a scholar of Puerto Rican economics.

According to Caraballo-Cueto, one of the board's recommendations to Judge Swain is to have 25 students per teacher. The recommendation states this is an ideal ratio, while reducing expenses. But "this is incorrect," Caraballo-Cueto said, explaining that because of Puerto Rico's diverse population that ratio should be lower. Although he acknowledged that the school system has seen a drop in enrollment, because of migration, Caraballo also said that the process used to determine which schools would close wasn't effective.

"There was no consultation with communities," he said. One of the major critics is that families now have to travel longer distances to take the kids to school. With the recent seismic movement another worry is being presented. School closures were not done taking in consideration which campuses were following the most recent construction code. With more than 900 earthquakes the island has seen in recent weeks some of the schools that were left opened were following the criteria of a construction code that had already been revised. The Agripina Seda school in Guánica collapsed after the 6.4 magnitude earthquake struck the island the morning of January 7th.

Right after the 6.4 earthquake, the Secretary of Education, Eligio Hernández, said that almost 95% of the schools in the island don't follow the newest construction code.

Funding cuts for the University of Puerto Rico has also become the norm. This includes reduced financing for Puerto Rico's Seismic Network, which is part of the university -- a reduction that has caused worry among Puerto Ricans, since right now they need to rely on the network to understand and monitor the surprising seismic movements in Puerto Rico.

At the same time, tuition for university students has risen.

"Rate increases are being used to pay a debt we didn't create," said Bigio, who says her tuition bills have risen from \$56 per credit in 2016 to \$116 per credit to this year. The University of Puerto Rico has a debt of nearly [\\$500 million](#).

Bigio has seen students drop out of school because they don't have the money to pay for their education, she says. "Austerity measures have forced them to become employees first and then students," she said.

From 2010 to 2016, according to the Education Council of Puerto Rico, the island has seen [a 7% reduction of public college students](#).

“Part of the ceiling in some classrooms are falling apart,” Bigio said.

Economists are worried about education cuts because in a deprived economy, they say, education becomes an even more important asset for a community struggling to survive. “Education is the key to get out of the crisis,” said Alba Brugueras, former president of Puerto Rico’s Economist Association.

One of the oversight board’s suggestions to improve the university’s financial health is to close some of the 11 campuses across the island. The problem is that each campus has its own expertise.

The Utuado campus, in the central-west part of the island, is among the ones at risk. It works with the local agriculture industry, and economists are worried that the campus closure could disrupt Utuado’s economy. “It could collapse,” said Heriberto Martínez, president of the economist association.

Student leaders at the university have organized to advocate for more funding.

“We have to invest in the university for it to run more effectively,” said Lyvan A. Buntin-Rivera, a student representative of the university who testified in October at the hearing held on PROMESA’s progress by the House’s Natural Resources Committee.

For bond researcher Cate Long, the decreased funding for education is extreme. “I haven’t seen cuts like these in any state university,” she said.

The poor and unstable conditions in education and other sectors have helped increase the numbers of people leaving the island, especially within the younger generation and the working class.

And as people flee from Puerto Rico in chunks, the board has continued to restructure the debt at a time when there are fewer taxpayers to help pay down the balance.

“You just have to buy an airplane ticket to disconnect from the debt,” said the Economist Association’s Martinez.

The most recent data from the U.S. Census Bureau shows there are 3.2 million people living on the island, compared to 3.5 million people before PROMESA was signed. At least 40% of the remaining population is more than 50 years old.

This has created concern among Puerto Ricans, since almost half of the people on the island are heading toward retirement.

Those retired from government work have suffered from cuts and could experience other reductions in the future.

At least 39% of the 167,000 pensioners could see cuts, as a way to repay and restructure the nearly \$55 billion debt in the retirement system, according to the Official Committee of Retirees. This amount is separate from the central government's debt.

The oversight board proposed a 8.5% cut to pensions that the new governor, Wanda Vázquez, has supported. "It's the best alternative in this crossroads," she said, in a video released by her office in September. These cuts must be voted on by pensioners and bondholders before Judge Swain can approve them. And the Puerto Rican legislature must pass specific fiscal laws and vote "yes" on the cuts to enact them.

There is still no designated date for this vote. Following the island's latest seismic events it's expected that any determination will be delayed.

Such legislative approval is crucial, said PROMESA expert Emmanuelli. "It's the only power Puerto Rico still has," he said.

For Lourdes Ramos and other members of the House of Representatives of Puerto Rico, cuts are not an option. "Discounts to pensioners are not happening," Ramos said.

Recently, the legislature passed a resolution that says no proposed pension cuts will be passed. "We already said that such a project will not be approved," Ramos said.

But political uncertainty may rise in 2020. "The game can change," Emmanuelli said.

If the legislature shifts, after the Puerto Rican general elections in November, legislators could "start working in favor of the board," Emmanuelli said. And because a fiscal plan hasn't yet been approved by Judge Swain, the oversight board can amend its decisions and recommendations.

Pensioners are using this delay to strengthen their "no cuts" campaign at demonstrations and on social media. "They are trying to erase us from the map," said Myra Rivera, who retired as a teacher eight years ago. "We have to resist and fight."

## What's next for the island?

A [rise in the cost](#) of living since the fiscal crisis started has become the new normal.

Monthly water bills from Puerto Rico's Aqueducts and Sewers Authority (a utility known as AAA in Spanish) have added a \$2.85 fee dedicated to subsidize the restructuring plan made by the board to meet the demands of the cuts imposed by them.

Like the water utility, Puerto Rico's Electric Power Authority (PREPA) has the same fee. Although there is already a designated payment for PREPA's fiscal plan, it's expected that rates will continue to rise.

For Puerto Ricans, this is seen as something outrageous since there is no stability in the electric grid.

Constant blackouts in Puerto Rico are "normal" on the island, especially after Hurricane María hit the island. Some people spent almost a year without power.

With a \$9 billion debt and an unstable electric grid -- Puerto Ricans refer to it as a "junker" -- the power authority is now facing another threat. One of the most important plants on the island suffered extreme damage with the recent earthquakes. "Costa Sur is a disaster," said PREPA CEO José Ortiz, referring to a power plant that generates at least 30% of the island's electricity. It will be out of service for more than a year.

Ricardo Ramos, former executive director of PREPA, says that an investment of millions of dollars is needed to get the authority back on track. He compares Puerto Rico's electrical grid to a classic car. "If you maintain it you can use it, but it wastes fuel like crazy," he said.

For more than a decade, PREPA hasn't been profitable. "Why not sell it?" said Representative Don Young, a Republican member of the House Natural Resources Committee, during its October hearing on PROMESA's progress.

Former Governor Rosselló announced in 2018 that the government was looking to sell PREPA's generation business as a public-private enterprise.

"PREPA doesn't have money," said Ramos, the agency's former head. The reason to sell, he says, is to get investment and buy new and innovative machinery.

“It’s an animal we have to kill,” said economist Vicente Feliciano, explaining that selling PREPA is key to an economic recovery. Because it is the only energy resource on the island, some economists consider its generation level to be an economic index and say that the sale of PREPA’s generation unit could bring jobs and investment to the island.

While there are hopes that someone could buy the \$4.5 billion generation system, some fear it is not attractive to buyers.

The system accounts for 50% of PREPA’s debt.

Other government agencies owe billions of dollars as well. Although there is a total approximate number of more than \$70 billion, the exact amount of debt is unclear.

“We should have audited the debt,” Bigio said, echoing the criticisms held by many in Puerto Rico ever since former Governor Alejandro García Padilla said the famous words “the debt is unpayable” in July 2015.

Fourteen months later, the board was appointed having one of the first meetings in New York City. “The board is there as a condition of Congress,” García Padilla said.

Although the board has been working with the restructuring of the island’s total debt of more than \$120 billion dollars, including pensions, there is still uncertainty of their performance.

“We have doubts about transparency and about the numbers,” Emmanuelli said.

The board did not respond to a request for comment.

Conversely others in the financial community are more positive. Matt Fabian, an analyst in the independent firm Municipal Market Analytics, says the oversight board has been moving forward, considering the island’s dense and complicated economic scenario. “I’ve been surprised that it is going as fast as it is,” he said.

He estimates the board’s work will continue for at least five more years. But the recent natural disasters on the island, along with the presidential election and impeachment trial of President Trump in the U.S., might change that forecast.

Add to that the damage and the effects of the recent earthquakes, which have only deepened people’s intentions to leave the island, intensifying the migration problem.

“I’m leaving, I’m not staying,” said Nidia Nazario, a 54-year-old nurse who lives in Guánica and is a victim of the quakes. After Hurricane María she was one of the 123,000 of Puerto Ricans who fled the island between 2017 and 2018 looking for stability. Although she found it in her daughter’s home in Florida, a couple of months later she moved back to the island because she wanted to be in her house.

Now things are completely different. “The house is not a priority right now,” she said.

Nazario is among the more than 8,000 people who have been living outside their houses for fear of a bigger earthquake or a tsunami.

### **Is PROMESA the right solution?**

Observations by some local experts include that PROMESA was not the best alternative for Puerto Rico’s future. But options were limited. Because the island had been excluded from restructuring or bankruptcy options that are only available for U.S. states, the bubble burst was more like a bomb.

When the situation got complicated back in 2016, then-Governor. Garcia-Padilla went to the U.S. Congress -- to seek what was best for Puerto Rico, he said. Although he didn’t want to have a fiscal oversight board, he says. that was the option he had to file bankruptcy.

“I asked for an ambulance with specifications, but when the ambulance arrived, Congress had sent another one,” said García Padilla, explaining that he asked the federal government what Puerto Rico needed, but they didn’t comply. “It came down to, do I get the patient on board or do I leave him to die,” he said.

Years later, the patient is alive but in critical condition, economists say.

Even though Hector Cordero-Guzman professor at Baruch College of the City University of New York agrees that this gave the island a “partial breath,” he says the federal government’s lack of action has contributed to the crisis.

“Congress hasn’t had the interest or the knowledge in how to help Puerto Rico,” he said.

At the same time, he doesn’t dismiss the role of Puerto Rico’s bondholders and other investors.

“They are allies of this crisis,” he said, explaining that local bondholders advocated in favor of the board at the beginning. Now, as the crisis deepens, even these bondholders have opposed to many of the board’s proposed cutbacks, leading to litigation between both sides.

Among those against the board’s actions are some Congress members. “I do not see progress,” said Tom McClintock, a Republican representative from California, who serves in the Natural Resources Committee.

Lack of progress is the biggest worry multiple economists have. “If there is no long-term plan, we will come back to a deprived economy,” Caraballo-Cueto said. If Puerto Rico doesn’t find a way to change the economic equation, he and others say, the island will fall into another crisis once they survive this one.

For Bigio, is no different. She knows every post published in her social media is her way of trying to make conscious. “At this pace, once the board ends there will not be a Puerto Rico,” she said.