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The Perfect Storm: Weathering Puerto Rico's Fiscal Crisis in the Wake of Hurricane Maria

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NOTE

THE PERFECT STORM: WEATHERING PUERTO RICO'S FISCAL CRISIS IN THE WAKE OF HURRICANE MARIA

I. INTRODUCTION

The depths of Puerto Rico's current crisis extend beyond the Island's obliterated power grid, food insecurity, and ravaged roads.[1] With a forty-five percent poverty rate, insolvent public pensions, and a shrinking population, Puerto Rico is in financial crisis mode.[2] In addition to the economic and fiscal crisis, Puerto Rico is confronting a massive humanitarian disaster.[3] On September 20, 2017, Hurricane Maria slammed into the Island and became the most destructive storm to hit Puerto Rico in almost ninety years.[4] With 155 mile per hour winds, Hurricane Maria knocked out all electric power, destroyed more than 100,000 homes, and ruptured bridges and other public infrastructure.[5] The Category Four storm was so wide—300 miles—that it covered the Island in its entirety and dropped over two feet of rain.[6] Following Maria's wrath, the Island has faced an ongoing shortage of food, water, electricity, and medical services, with little signs of improvement.[7]

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1. Lauren Lluveras, *Puerto Rico's Bankruptcy Will Make Hurricane Recovery Even Harder*, WASH. POST (Sept. 27, 2017), https://www.washingtonpost.com/news/posteverything/wp/2017/09/27/puerto-ricos-bankruptcy-will-make-hurricane-recovery-even-harder/?utm_term=.87688915d935.

2. Stephanie Kelly, *Hedge Funds Disclose Their Puerto Rico Debt Holdings*, REUTERS (July 26, 2017), https://www.reuters.com/article/puertorico-debt/hedge-funds-disclose-their-puerto-rico-debt-holdings-idUSL1N1KH1FC.

3. *Id.*; Lluveras, *supra* note 1.

4. *Rating Action: Moody's Downgrades Puerto Rico GOs, COFINA and Other Debt After Hurricane Maria; Outlook Negative*, MOODY'S INVEST. SERV. (Oct. 11, 2017), https://www.moodys.com/research/Moodys-Downgrades-Puerto-Rico-GOs-COFINA-and-Other-Debt-After--PR_904269952.

5. Catesby Holmes, *Puerto Rico Two Months After Maria: 5 Essential Reads*, CONVERSATION (Nov. 19, 2017), http://theconversation.com/puerto-rico-two-months-after-maria-5-essential-reads-87409.

6. *Id.*

7. *Id.*

While Hurricane Maria escalated the Island's financial troubles, Puerto Rico's current fiscal state is derived from a multitude of sources.[8] The continuing population decline, overextension of municipal bonds, and oppressive social spending have forced the Island to seek assistance from the U.S. government to help relieve the Island of its pressing $70 billion debt.[9] Unable to seek relief under the U.S. Bankruptcy Code, Puerto Rico has been undergoing a restructuring effort under the newly promulgated Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA").[10]

Amidst the legal and political uncertainty of PROMESA and the catastrophic effects of Hurricane Maria, Puerto Rico's municipalities are currently attempting to restructure their immense sovereign debts while simultaneously attempting to recover from the catastrophic storm that destroyed thousands of businesses and homes.[11] This Note analyzes the various economic issues currently plaguing Puerto Rico, as well as the compounding ramifications as a result of Hurricane Maria.[12] Part II presents a brief history of Puerto Rico and the economic backdrop that has led the Island into its financial crisis.[13] Part III analyzes PROMESA and why the legislation was created as an alternative to Chapter 9 relief under the U.S. Bankruptcy Code.[14] Part III also breaks down the major features of Puerto Rico's restructuring process under Title III of PROMESA including its various sources of debt types, main creditors, and current litigation.[15] Furthermore, Part III details the compounding economic effects as a result of Hurricane Maria.[16] Part IV discusses possible solutions to Puerto Rico's longstanding fiscal problems that have plagued the Island for decades.[17] This Part offers suggestions that can help afford Puerto Rico independent financial standing by amending PROMESA and offering new tax initiatives that will simultaneously incentivize local and corporate growth on the Island.[18] Finally, this Note

8. Heather Long, *Puerto Rico's Crisis: How Did It Get So Bad?*, CNN: MONEY (May 12, 2016, 12:58 PM), http://money.cnn.com/2016/05/12/investing/puerto-rico-debt-crisis/index.html.

9. *Id.*

10. Andrés L. Córdova, *PROMESA and Puerto Rico's Political Future*, HILL (July 14, 2017, 8:30 AM), http://thehill.com/blogs/congress-blog/politics/341949-promesa-and-puerto-ricos-political-future; *see also* Steven Mufson, *Shaky Puerto Rican Dam Has Gone Uninspected Since 2013*, WASH. POST, Sept. 27, 2017, at A6.

11. Córdova, *supra* note 10.

12. *See infra* Parts II–IV.

13. *See infra* Part II.

14. *See infra* Part III.

15. *See infra* Part III.C.

16. *See infra* Part III.D.

17. *See infra* Part IV.

18. *See infra* Part IV.

concludes by discussing why Puerto Rico's financial restructuring and pressing humanitarian issues are so significant.[19]

II. A BRIEF HISTORY OF PUERTO RICO

A. *Puerto Rico's Constitutional Status*

The United States acquired Puerto Rico, Guam, and the Philippines from Spain via the Treaty of Paris, signed in 1898.[20] Puerto Rico is a U.S. territory subject to congressional authority derived from the Territory Clause of the U.S. Constitution.[21] The Territory Clause grants Congress the "[p]ower to dispose of and make all needful Rules and Regulations respecting the Territory or other Property belonging to the United States."[22] While the Jones Act of 1917 granted U.S. citizenship to Puerto Ricans, Puerto Ricans are not afforded the same protections as U.S. citizens residing in the States.[23] Namely, Puerto Ricans lack voting representation in Congress and the ability to vote in presidential elections.[24]

Puerto Rico has historically struggled to maintain a strong and independent economy and has depended on U.S. tax breaks to incentivize business growth.[25] The U.S. federal government has attempted to encourage business development in Puerto Rico on multiple occasions by offering corporate tax exemptions.[26] Implemented in 1976, section 936 of the Internal Revenue Code provided significant incentives for U.S. corporations to locate subsidiaries on the Island by allowing a subsidiary "more [than] 80% owned by a foreign entity to deduct 100%

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19. *See infra* Part V.

20. R. SAM GARRETT, CONG. RESEARCH SERV., R44721, POLITICAL STATUS OF PUERTO RICO: BRIEF BACKGROUND AND RECENT DEVELOPMENTS FOR CONGRESS 2 (2017). The weight of importance of Puerto Rico's status as a territory is often heavily debated among scholars. *Id.* at 3-4. Some believe that the debate of Puerto Rico's statehood status is a distraction from the longstanding issues plaguing the Island. *Id.* Others, however, believe that the Island's distinction from statehood status is the foundation from which most of the Island's financial issues can be traced back to. *Id.* While it is important to note the legal significance of Puerto Rico as a territory or commonwealth, the debate regarding the future statehood of Puerto Rico is outside the scope of this Note. *Id.*

21. *Id.* at 4.

22. U.S. CONST. art. IV, § 3, cl. 2.

23. Perry T. Graham, *Municipal Bankruptcy in "the Oldest Colony in the World" After* Puerto Rico v. Franklin California Tax-Free Trust *and PROMESA*, 63 LOY. L. REV. 179, 186 (2017).

24. *Id.*

25. Scott Greenberg & Gavin Ekins, *Tax Policy Helped Create Puerto Rico's Fiscal Crisis*, TAX FOUND. (June 30, 2015), https://taxfoundation.org/tax-policy-helped-create-puerto-rico-s-fiscal-crisis.

26. *Id.*

of the dividends paid to its parent."[27] Subsidiaries in Puerto Rico, therefore, paid no corporate income tax as long as their profits were distributed as dividends.[28] As a result of "these generous tax incentives for businesses, Puerto Rico grew rapidly throughout the twentieth century and developed a substantial manufacturing sector, though it remained relatively poor compared to the U.S. mainland.[29]

In 2006, Congress allowed for the tax incentives for corporate operations to expire as many individuals viewed these incentives as a way to avoid taxes, referring to the law as "the mother of all tax shelters."[30] The expiration of these benefits has troubled the Island's job market as businesses elected to discontinue their presence in Puerto Rico.[31] With businesses leaving the Island, Puerto Rico's residents have followed in increasing numbers.[32] Since 2005, Puerto Rico has lost roughly ten percent of the population.[33] Making matters worse, Puerto Rico has an extremely low labor participation rate, with only forty percent of the adult population employed or looking for work.[34] As the population shrinks below 3.5 million, the reduction of its tax base heightens the Island's revenue crisis.[35]

B. Issuance of Bonds and Resulting Debt

In 1917, Congress allowed the Commonwealth of Puerto Rico "to issue municipal bonds tax-free from all U.S. federal, state and local governments."[36] The interest derived on most municipal bonds is subject to taxes by various levels of government.[37] Therefore, the triple tax-

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27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.*; *see* Nick Brown, *How Dependence on Corporate Tax Breaks Corroded Puerto Rico's Economy*, REUTERS (Dec. 20, 2016, 12:00 PM), http://www.reuters.com/investigates/special-report/usa-puertorico-economy.

31. Greenberg & Ekins, *supra* note 25.

32. Nick Timiraos, *Puerto Rico's Drastic Population Loss Deepens Its Economic Crisis*, WALL ST. J. (June 29, 2016, 7:35 PM), https://www.wsj.com/articles/puerto-ricos-drastic-population-loss-deepens-its-economic-crisis-1467219467.

33. *Id.*

34. ANNE O. KRUEGER, RANJIT TEJA & ANDREW WOLFE, PUERTO RICO – A WAY FORWARD 6 (2015).

35. *Id.* at 7.

36. Bradley Wendt, *Puerto Rico Fiscal Reform: The End of the Beginning*, LAW360 (June 14, 2017, 1:01 PM), https://www.law360.com/articles/934550/puerto-rico-fiscal-reform-the-end-of-the-beginning.

37. Greg DePersio, *The Origins of the Puerto Rican Debt Crisis*, INVESTOPEDIA (May 31, 2017, 8:42 AM), http://www.investopedia.com/articles/investing/090915/origins-puerto-rican-debt-crisis.asp.

exempt status made Puerto Rico's bonds highly appealing to U.S. investors at a very low cost for the Commonwealth.[38]

Puerto Rico has had a history of questionable budget balancing procedures.[39] Whereas many state constitutions provide "strict [and] explicit balanced budget requirements to ensure that expenditures in a fiscal year are within the cash available for that fiscal year," the Puerto Rican Constitution does not confer strict requirements on its municipalities to produce balanced budgets.[40] In 1952, Congress approved Puerto Rico's new Constitution that relaxed balanced budget requirements.[41] However, Congress's approval to loosen Puerto Rico's borrowing capacity was less based in policy and more of a translation issue.[42] The 1952 Puerto Rico Constitution was passed in English.[43] Specifically, the English version stated: "appropriations made for any fiscal year shall not exceed the total revenues, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."[44] However, in the Spanish text, the English term "total revenues" was translated as "*recursos totales*."[45] Lacking a direct translation, the phrase "*recursos totales*" was argued by Puerto Rican delegates to mean "total resources"; a concept broader than simply "revenues."[46] The broader interpretation "included revenues from taxation, surpluses, royalties, federal assistance, and, most importantly, funds obtained through the sale of bonds."[47]

A subsequent constitutional amendment in 1961 loosened the reins of debt capacity.[48] In 1961, Congress amended the Puerto Rico Federal Relations Act to remove the federally imposed debt limit based on assessed valuation.[49] Prior to the amendment, "[m]unicipalities were allowed to borrow between 5 and 10 percent of assessed value on their own, without including commonwealth debt in the calculation."[50]

38. *See* Wendt, *supra* note 36.
39. *See id.*
40. NAT'L CONFERENCE OF STATE LEGISLATURES, NCSL FISCAL BRIEF: STATE BALANCED BUDGET PROVISIONS 2-5 (2010).
41. MARC D. JOFFE & JESSE MARTINEZ, ORIGINS OF THE PUERTO RICO FISCAL CRISIS 8 (2016).
42. *Id.* at 10-11.
43. *Id.*
44. *Id.*
45. *Id.* at 11.
46. *Id.* (statement of Delegate Negrón López).
47. *Id.*
48. *Id.* at 12.
49. *Id.* at 12-13.
50. *Id.* at 13.

Following the amendment, the Commonwealth no longer had a debt limit based on assessed valuation and instead "the amendment imposed a 15 percent ceiling on *debt service* (principal and interest payments) as a percentage of tax revenues."[51] The borrowing limit only applied to "bonds or notes for the payment of which the full faith credit and taxing power of the Commonwealth shall be pledged" and therefore did not apply to bonds backed by a single tax.[52] Ultimately, the Puerto Rican government utilized this amendment to create a loophole by forming *Corporación del Fondo de Interés Apremiante* ("COFINA"), an entity that issues bonds backed exclusively by the Commonwealth's sales tax revenues and which are not included in the debt limit.[53]

The broader interpretation of "revenues," coinciding with the relaxed debt capacities, allowed debt proceeds to be used as a tool to balance the budget, which allowed for recurring operating deficits.[54] The loosening, in turn, encouraged Puerto Rico to fund fiscal shortfalls through the issuance of the triple-exempt municipal bonds.[55] Puerto Rico issued extensive bond debt and began relying on borrowed funds from the bond issuance to balance its budget and not actual revenue.[56] This practice led to a widening budget deficit.[57] Puerto Rico's debt represents nearly seventy percent of the territory's gross domestic product.[58] Comparatively, states in the U.S. only have a seventeen percent debt-to-GDP ratio on average.[59]

Aside from taxes on the sale of bonds, Puerto Rico also has a major issue collecting taxes.[60] A 2015 study by KPMG reported that Puerto Rico collects just fifty-six percent of the sales taxes due.[61] Although Puerto Rico has attempted to tackle tax evasion by passing legislation requiring merchants to take other payment forms in addition to cash, professional offices such as doctors continue to charge on a cash only basis in an effort to avoid taxes and post signs that read: "No Checks, No Credit Cards, No ATM Cards. Just Cash."[62]

51. *Id.*
52. *Id.*
53. *Id.*
54. *Id.* at 11.
55. *Id.* at 15.
56. *Id.*
57. *Id.*
58. DePersio, *supra* note 37.
59. *Id.*
60. Greg Allen & Marisa Peñaloza, *In Puerto Rico's Debt Crisis, There Are No Easy Solutions*, NPR (May 5, 2015, 4:29 PM), https://www.npr.org/2015/05/05/403290738/in-puerto-ricos-debt-crisis-there-are-no-easy-solutions.
61. *Id.*
62. *Id.*

As a result of the Commonwealth's escalating debt, three major credit rating agencies downgraded Puerto Rico's debt to junk status in 2014.[63] This poor investment grade status triggered acceleration clauses in contracts with many of the territory's creditors.[64] With principal and interest payments due sooner than expected, Puerto Rico's revenues proved insufficient to pay the obligations.[65] The Commonwealth's $74 billion debt consists of $17.8 billion of general obligation and Commonwealth-guaranteed bonds, $17.6 billion of COFINA bonds, $9 billion in Puerto Rico's Electric Power Authority ("PREPA"), $52.2 billion of pension-related debt owed to current and future retirees, and $20.8 billion of other related debt, including debt of the Government Development Bank, the water utility and highway agency, and the University of Puerto Rico.[66] As of October 2017, the Commonwealth has a pension liability of $49 billion owed to current and future retirees.[67]

C. *Attempted Economic Legislation*

After the tax breaks expired for mainland U.S. manufacturers in 2006, Puerto Rico attempted to combat its plagued economy through legislation meant to incentivize business growth.[68] In 2008, Puerto Rico passed the Economic Incentives for the Development of Puerto Rico Act ("EIA").[69] The EIA provided tax credits and incentives designed to encourage the establishment and development of various enterprises, including manufacturing, commercial business, and Internet-based operations.[70]

In 2012, Puerto Rico enacted further initiatives to promote the exportation of services by providing attractive tax incentives for companies that establish and expand their export service businesses in the Island, which included a 4% corporate tax rate, 100% tax exemption on dividends or profit distributions, and 100% exemption on property taxes.[71] Furthermore, Act No. 22 of 2012 sought to "attract new

63. *See* DePersio, *supra* note 37.

64. *Id.*

65. *Id.*

66. *Puerto Rico Debt Crisis: Making Sense of the Debacle*, BLOOMBERG NEWS, https://www.bloomberg.com/graphics/2017-puerto-rico-debt-crisis (last updated Oct. 4, 2017).

67. *Id.*

68. *Puerto Rico Tax Incentives*, SOTHEBY'S INT'L REALTY, http://puertoricotaxincentives.com (last visited Apr. 15, 2018).

69. *See* Economic Incentives Act for the Developlment of Puerto Rico, 2008 P.R. Laws No. 73; *Puerto Rico Debt Crisis*, *supra* note 68.

70. *Puerto Rico Tax Incentives*, *supra* note 68.

71. *Id.*

residents to Puerto Rico by providing a total exemption from Puerto Rico income taxes on all passive income realized or accrued after such individuals become bona fide residents of Puerto Rico."[72] This relocation exemption sought to accelerate the Island's economy by increasing investments in real estate services, and other consumption products, and in capital injections.[73]

The tax legislation, however, proved to be insufficient to incentivize business growth in the long term as businesses continue to retreat out of Puerto Rico.[74] Rather, the legislation reflects Puerto Rico's longstanding economic policies, which have tended to favor outside corporations over local businesses.[75] Critics have argued that the continued tax breaks only promote an artificial economic stability and reflect Puerto Rico's historical dependence on mainland corporations.[76]

III. Fiscal Restructuring Under PROMESA and the Effect of Hurricane Maria

Chapter 9 of the U.S. Bankruptcy Code (the "Code") offers protections to a financially distressed municipality "from its creditors while it develops and negotiates a plan for adjusting its debts."[77] Reorganization of the debts of a municipality is generally "accomplished either by extending debt maturities, reducing the amount of principal or interest, or refinancing the debt by obtaining a new loan."[78] Although there are some similarities to other chapters of the Code, Chapter 9 is vastly different in some respects.[79] Under Chapter 9, "there is no provision in the law for liquidation of the assets of the municipality and distribution of the proceeds to creditors" in that "such a liquidation or dissolution would undoubtedly violate the Tenth Amendment to the Constitution and the reservation to the states of sovereignty over their internal affairs."[80] Furthermore, the functions of the bankruptcy court in Chapter 9 cases are usually limited "to approving the petition, . . . confirming a plan of debt adjustment, and ensuring implementation of the plan."[81]

72. *Id.*
73. *Id.*
74. *See* Brown, *supra* note 30.
75. *Id.*
76. *Id.*
77. *Chapter 9 – Bankruptcy Basics*, U.S. CTS., http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-9-bankruptcy-basics (last visited Apr. 15, 2018).
78. *Id.*
79. *Id.*
80. *Id.*
81. *Id.*

Although Puerto Rico was originally expressly eligible for relief under Chapter 9 of the Code, Congress amended the Code in 1984 without comment, barring Puerto Rico and the District of Columbia from authorizing their municipalities to access Chapter 9.[82] Ineligible for relief under the Code, in 2014 Puerto Rico responded to the ongoing fiscal crisis by enacting the Puerto Rico Corporation Debt Enforcement and Recovery Act (the "Act").[83] The Act enabled Puerto Rico's public utility companies to implement a restructuring plan for its debt.[84] In 2016, however, the Supreme Court decided that the Code preempted the Act.[85] This preemption prompted the creation of PROMESA by Congress; the vehicle that Puerto Rico is currently utilizing to restructure its massive debt.[86]

Subpart A discusses the federal preemption that led to the creation of PROMESA.[87] Subpart B describes the major characteristics of PROMESA.[88] Subpart C outlines the ongoing proceedings of current municipalities adjusting their debts under Title III of PROMESA by describing the various kinds of debt and creditors.[89] Finally, Subpart D details the devastating effect that Hurricane Maria has had on the Island as well as its compounding economic effects on the ongoing restructuring process.[90]

A. Puerto Rico's Status as a "State" for Purposes of the Code

In 2016, the Supreme Court analyzed the applicability of the Code in Puerto Rico.[91] Here, a group of bondholders holding $2 billion in PREPA bonds sought to enjoin the application of the Act, arguing, inter alia, that while Puerto Rico should not fall within the definition of a "State" under the Code's "gateway" provision, Puerto Rico could be considered a "State" for section 903(1) of the Code.[92] Section 903(1) of the Code preempts a state from enacting its own bankruptcy laws that enable insolvent municipalities to restructure their debts over the objections of creditors, and instead requires municipalities to restructure

82. 11 U.S.C. § 101(52) (2012); Adam Liptak & Mary Williams Walsh, *Justices Reject Puerto Rico in Case on Restructuring Debt*, N.Y. TIMES, June 14, 2016, at B3.

83. Liptak & Walsh, *supra* note 82.

84. *Id.*

85. *Id.*

86. *Id.*

87. *See infra* Part III.A.

88. *See infra* Part III.B.

89. *See infra* Part III.C.

90. *See infra* Part III.D.

91. Puerto Rico v. Franklin Cal. Tax-Free Trust, 136 S. Ct. 1938 (2016).

92. *Id.* at 1943, 1946.

their debts under Chapter 9.[93] Section 109(c) of the Code, often referred to as the "gateway" provision, defines the definition of "Debtor" for purposes of who may be authorized to seek relief under Chapter 9 of the Code.[94]

The Court agreed with the bondholders and found that the Puerto Rico Recovery Act was preempted by section 903(1).[95] The Supreme Court found that while Puerto Rico was ineligible for relief under the Code in that Puerto Rico is not a "State" for purposes of the Code's "gateway" provision, Puerto Rico is considered a "State" for purposes of the Code's preemption provision.[96] The Court stated that the "amended definition of 'State' excludes Puerto Rico for the single 'purpose of defining *who may be a debtor* under chapter 9'" and that it therefore "interpret Congress' use of the 'who may be a debtor' language in the amended definition of 'State' to mean that Congress intended to exclude Puerto Rico from this gateway provision delineating who may be a debtor under Chapter 9."[97] The Court reasoned, however, that

> Puerto Rico is no less bound by the pre-emption provision even though Congress has removed its authority to provide authorization for its municipalities to file Chapter 9 petitions [in that] if it were Congress' intent to also exclude Puerto Rico as a "State" for purposes of that pre-emption provision, it would have said so.[98]

Further, the fact "[t]hat Puerto Rico is not a 'State' for purposes of the gateway provision, however, says nothing about whether Puerto Rico is

93. 11 U.S.C. § 903 (2012) ("This chapter does not limit or impair the power of a State to control, by legislation or otherwise, a municipality of or in such State in the exercise of the political or governmental powers of such municipality, including expenditures for such exercise, but—(1) a State law prescribing a method of composition of indebtedness of such municipality may not bind any creditor that does not consent to such composition; and (2) a judgment entered under such a law may not bind a creditor that does not consent to such composition.").

94. *Id.* § 109(c) ("An entity may be a debtor under chapter 9 of this title if and only if such entity—(1) is a municipality; (2) is specifically authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter; (3) is insolvent; (4) desires to effect a plan to adjust such debts; and (5)(A) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter; (B) has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter; (C) is unable to negotiate with creditors because such negotiation is impracticable; or (D) reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under section 547 of this title.").

95. *Puerto Rico*, 136 S. Ct. at 1949.

96. *Id.* at 1947.

97. *Id.* at 1946.

98. *Id.* at 1948.

a 'State' for the other provisions of Chapter 9 involving the States," and therefore the Act was preempted by Code section 903(1).[99]

In the 5-2 opinion, Justice Thomas reasoned that the decision was compelled by a straightforward reading of the federal law, which "bars Puerto Rico from enacting its own municipal bankruptcy scheme to restructure the debt of its insolvent public utilities companies."[100] In dissent, however, Justice Sonia Sotomayor argued that the majority's approach was too mechanical, and failed to take into account the purpose of the bankruptcy law and the impact of its decision.[101] By preempting the Restructuring Act, Sotomayor argued that the Court ignored the realities of Puerto Rico's crisis as it takes away "the only existing legal option for Puerto Rico to restructure debts that could cripple its citizens."[102]

B. Enactment of PROMESA

Shortly following the Supreme Court's ruling, in June 2016 Congress quickly enacted legislation to respond to Puerto Rico's ongoing economic crisis.[103] PROMESA established a process for restructuring Puerto Rico's public debt.[104] Title III of PROMESA, like the Code, includes a provision for a plan of adjustment to be proposed by the debtor, voted on by creditors and confirmed by the court.[105] United States District Judge Laura Taylor Swain, for the Southern District of New York, was designated by Supreme Court Chief Justice John Roberts to preside under the Title III cases pending in the United States District Court for the District of Puerto Rico.[106]

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99. *Id.* at 1947.

100. *Id.* at 1942.

101. *Id.* at 1953-54 (Sotomayor, J. dissenting).

102. *Id.* at 1949-50. Justice Sotomayor went on to foreshadow the electrical blackouts by describing the importance of the particular debt stating:

> The Commonwealth of Puerto Rico and its municipalities are in the middle of a fiscal crisis. The combined debt of Puerto Rico's three main public utilities exceeds $20 billion. These utilities provide power, water, sewer, and transportation to residents of the Island. With rising interest rates and limited access to capital markets, their debts are proving unserviceable. Soon, Puerto Rico and the utilities contend, they will be unable to pay for things like fuel to generate electricity, which will lead to rolling blackouts. Other vital public services will be imperiled, including the utilities' ability to provide safe drinking water, maintain roads and operate public transportation.

Id.

103. *See* GARRETT, *supra* note 20, at 16.

104. *Id.*

105. D. ANDREW AUSTIN, CONG. RESEARCH SERV., R44532, THE PUERTO RICO OVERSIGHT, MANAGEMENT, AND ECONOMIC STABILITY ACT (PROMESA; H.R. 5278, S. 2328) 4 (2016).

106. Cate Long, *Developing: Puerto Rico Enters Bankruptcy on May 3*, 36 AM. BANKR. INST. J. 12, 86 (2017).

Modeled after Chapter 9 of the Code, PROMESA creates a structure for exercising federal oversight over the fiscal affairs of the territory by establishing an Oversight Board with broad powers of budgetary and financial control, procedures for adjusting debts accumulated by the Puerto Rican government and its instrumentalities, and expedites approval of key energy and "critical projects" in Puerto Rico.[107] The Oversight Board consists of seven members appointed by the President of the United States and one *ex-officio* member designated by the Governor of Puerto Rico.[108] "The Oversight Board operates as an entity within the Puerto Rican Government, and is given broad authority over the Commonwealth and any of its instrumentalities that the Board designates as 'covered' instrumentalities."[109] Furthermore,

> the Board is endowed with a variety of significant powers, including the authority to develop, review, and approve territorial and instrumentality fiscal plans and budgets; to enforce budget and fiscal compliance; to seek judicial enforcement of its authority to carry out its responsibilities under PROMESA; and to intervene in any litigation filed against the Commonwealth or its instrumentalities.[110]

Title III does not impair or limit the territory's power to control itself or its instrumentalities and permits the operations of the municipalities to continue functioning uninterrupted.[111] Thus, government facilities will remain open, employees will continue to receive regular wages and benefits, and government services will continue to be provided.[112] To emerge from Title III, each debtor must file a plan of adjustment that will provide for the classification and adjustment of the debtor's debts.[113]

C. *Current Status of Title III of PROMESA*

Under Title III, Puerto Rico is currently unraveling the $74 billion debt owned by creditors including bondholders and pension plan holders.[114] Untangling the web of securities sold by various agencies and secured by numerous types of revenue funds from taxes to tolls has

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107. AUSTIN, *supra* note 105, at 1, 6, 15.

108. *Id.* at 3.

109. Puerto Rico Oversight, Management, and Economic Stability Act, 48 U.S.C. § 2121 (2016); Brigade Leveraged Cap. Structures Fund Ltd., v. Garcia-Padilla, 217 F. Supp. 3d 508, 514 (D.P.R. 2016).

110. *Brigade Leveraged Cap. Structures*, 217 F. Supp. 3d at 514 (citations omitted).

111. *See* Long, *supra* note 106, at 83.

112. *Id.*

113. *Id.*

114. *See Puerto Rico Debt Crisis: Making Sense of the Debacle*, *supra* note 66.

raised various issues with regard to the constitutionality by which the securities were issued.[115] As Puerto Rico's municipalities move through Title III, the Oversight Board is tasked with creating and implementing a fiscal plan that will seek to reduce consolidated government spending, boost revenue, and lead Puerto Rico into long-term fiscal stability.[116] Simultaneously, the Oversight Board must coordinate the cooperation of its major creditors and various debt related lawsuits.[117]

1. Types of Creditors

While the Commonwealth has a variety of creditors, the dominant creditors are the Puerto Rico Sales Tax Financing Corporation bondholders and general obligation bondholders.[118] COFINA bonds are non-recourse bonds that are paid solely from, and secured by the sales and use tax.[119] General obligation bond payments are not linked to one specific revenue source and are guaranteed by the Island's Constitution.[120] Thus, COFINA and general obligation bondholders are beginning to battle for the first claim on the Commonwealth's sales tax revenue.[121] About thirty percent of the Commonwealth's $74 billion debt is owned by hedge funds.[122]

Although big institutional investors and hedge funds own a significant portion of the $74 billion of Puerto Rico's outstanding bonds, "two-thirds of the debt is held by retail investors, either outright or in one of the dozens of U.S.-based retail municipal-bond funds."[123] Additionally, bond-insurance companies that guarantee a significant portion of Puerto Rico's debt in the event of a default will also have a major stake throughout the restructuring proceedings.[124] The three biggest bond-insurers are Ambac Financial Group Inc., Assured

115. *Id.*

116. AUSTIN, *supra* note 105, at 11; *see* Brigade Leveraged Cap. Structures Fund Ltd. v. Garcia-Padilla, 217 F. Supp. 3d 508, 514 (D.P.R. 2016).

117. *Brigade Leveraged Cap. Structures*, 217 F. Supp. 3d at 514.

118. Lex Claims, LLC v. Fin. Oversight & Mgmt. Board, 853 F.3d 548, 550 (1st Cir. 2017).

119. *Id.* at 551 n.4; Katherine Burton, Rebecca Spalding, & Michelle Kaske, *Maria Made Puerto Rico's Giant Debt Even Trickier for Hedge Funds*, BLOOMBERG (Oct. 12, 2017), https://www.bloomberg.com/news/articles/2017-10-12/maria-made-puerto-rico-s-giant-debt-even-trickier-for-hedge-funds.

120. Burton, Spalding, & Kaske, *supra* note 119.

121. Kelly, *supra* note 2.

122. *See Puerto Rico Debt Crisis: Making Sense of the Debacle*, *supra* note 66.

123. Abby Schultz, *Puerto Rico's Debt Victims Aren't All Vulture Funds*, BARRON'S (Oct. 28, 2017), http://www.barrons.com/articles/puerto-ricos-debt-victims-arent-all-vulture-funds-1509159296.

124. *See Puerto Rico Debt Crisis: Making Sense of the Debacle*, *supra* note 66.

Guaranty Municipal Corp., and National Public Finance Guarantee Corp., a unit of MBIA Inc.[125]

2. Fiscal Adjustment Plan

While a keystone to the PROMESA process is the development of a five-year fiscal plan, the Oversight Board instead chose to develop a ten-year plan.[126] On March 13, 2017, the Oversight Board certified the ten-year fiscal plan for the Commonwealth's government.[127] The plan reduces consolidated government spending by five percent, pension costs by ten percent, and debt services by seventy-eight percent.[128] The plan

> aims to boost revenues with tax reforms, increase tax compliance and increase fees and taxes; tighten government spending with a wage freeze until 2020 and cut subsidies and operational expenditures; extract economics in health care spending and pension plans; and invest in infrastructure projects along with support from public/ private partnerships.[129]

The fiscal plan projected a $100 million reduction in fiscal year 2018 health care spending by capping payment to health care providers and decreasing pension costs by $83 million beginning in 2020.[130] Revenue enhancements in the fiscal plan depend primarily on the expansion of the reform of corporate taxes, extension of current sales tax to Internet purchasers, increase in excise taxes on tobacco products, and a ten percent increase in the cost of traffic fines.[131]

3. Debt Related Lawsuits

There are various debt related lawsuits that have arisen as a result of Puerto Rico's bankruptcy proceedings.[132] General obligation bondholders claim Puerto Rico's Constitution requires all sales-tax money be used to pay them instead of COFINA bondholders.[133] Hedge funds and bond insurers are competing for any monetary amount the government collects, including cash from rum taxes, vehicle fees, and

125. *Id.*
126. Long, *supra* note 106, at 12.
127. *Id.* at 77.
128. *Id.*
129. *Id.*
130. *Id.* at 78.
131. *Id.*
132. *Puerto Rico Debt Crisis: Making Sense of the Debacle*, *supra* note 66.
133. *Id.*

tolls.[134] COFINA bond insurer, Ambac Financial Group, has sought to overrule moratorium orders and legislation in effect since the end of 2015 that allow the government to "claw back" certain sources of income (taxes, cigarette licenses, oil barrel fees, etc.) that guarantee the payment of specific debt.[135] In its request, Ambac is attempting to prevent the government from appropriating sales and use tax funds that guarantee the payment of COFINA debt.[136]

D. Hurricane Maria's Devastating Impact

In the midst of its financial restructuring, on September 21, 2017, Hurricane Maria slammed into Puerto Rico; plunging the Island into darkness and forcing many of the 3.4 million citizens to confront life without their homes, electricity, or gas.[137] The Category Four storm wiped out the Island's power grid leaving the Island without power.[138] For virtually three weeks following the storm, there was a near total communication blackout.[139] Experts estimated that the hurricane demolished 100,000 homes and buildings, and ninety percent of the Island's infrastructure was deemed unsafe.[140] Two months after the storm, roughly 1520 people continued to live in shelters.[141] Economic losses are estimated to range between $30 billion to $95 billion after Hurricane Maria wiped out the Island's power grid and left inhabitants without running water and shortages of food and medicine.[142] The hurricane has had far-reaching consequences on population health as damaged infrastructure has isolated communities and left hospitals without supplies, overcrowding, and poor sanitation.[143] While the official death toll was initially certified as sixty-four, mounting evidence indicates that Puerto Rico vastly undercounted the number of deaths and that the total may actually be closer to 1052.[144]

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134. *Id.*

135. Long, *supra* note 106, at 84.

136. *Id.*

137. Lluveras, *supra* note 1.

138. Burton, Spalding, & Kaske, *supra* note 119.

139. Holmes, *supra* note 5.

140. *Id.*

141. Lydia O'Connor, *7 Numbers that Explain How Puerto Rico Is Still Suffering*, HUFFINGTON POST (Nov. 20, 2017, 7:30 PM), https://www.huffingtonpost.com/entry/puerto-rico-maria-by-the-numbers_us_5a134c85e4b0c335e996b89d.

142. Burton, Spalding, & Kaske, *supra* note 119.

143. Jennifer Sciubba & Jeremy Youde, *Puerto Rico's Troubles Are Far from Over. The Population's Health Is at Risk.*, WASH. POST (Oct. 13, 2017), https://www.washingtonpost.com/news/monkey-cage/wp/2017/10/13/puerto-ricos-troubles-are-far-from-over-the-populations-health-is-at-risk/?utm_term=.0e190bcdc43f.

144. Patricia Mazzei, *Puerto Rico Orders Review and Recount of Hurricane Deaths*, N.Y.

Businesses continue to struggle even weeks after the storm hit the Island.[145] The absence of power and Internet has crippled local commerce, which has been forced to rely on paper and cash in the absence of taking customer credit cards.[146] Similarly, hotels and local car-rental agencies have turned to written records to keep track of bookings.[147]

Moody's September Analytics Report has estimated that between $20 billion to $40 billion could be lost in productivity output due to storm related disruptions.[148] Most Puerto Rican bonds have collapsed in price since the storm.[149] For example, Puerto Rico's most recent offering, a $3.5 billion general-obligation bond due in July 2035 with an eight percent coupon, is trading for less than twenty-eight cents on the dollar.[150] Additionally, COFINA bonds are trading for approximately forty cents on the dollar.[151] As of October 11, 2017, Moody's Investor Services downgraded the Commonwealth of Puerto Rico's general obligation bonds from "Caa3" to "Ca," describing the storm's overall economic impact after the economic and revenue disruptions as a "substantial negative that has weakened the Commonwealth's ability to repay creditors."[152]

1. Government Contracts

As Puerto Rico continues to rebuild, the Puerto Rican government has come under immense criticism regarding the process by which contracts have been awarded. On September 26, 2017, Puerto Rico's utility company, PREPA, awarded a $300 million contract to Whitefish Energy to rebuild the Island's electrical grid.[153] Whitefish Energy is a two-year-old Montana-based company that had only two employees at the time that it was awarded the contract.[154] Critics have questioned the legitimacy of the contract that was granted without a public bid process

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TIMES (Dec. 18, 2017), https://www.nytimes.com/2017/12/18/us/puerto-rico-hurricane-maria-death-toll-review.html.

145. Daniela Hernandez & Arian Campo-Flores, *Puerto Rico's Economy Is Back to Basics*, WALL ST. J., Oct. 16, 2017, at A3.

146. *Id.*

147. *Id.*

148. *Id.*

149. Schultz, *supra* note 123.

150. *Id.*

151. *Id.*

152. *Rating Action: Moody's Downgrades Puerto Rico GOs, COFINA and Other Debt After Hurricane Maria; Outlook Negative*, *supra* note 4.

153. Richard Pérez-Peña, *'Significant Concerns' Cited over Puerto Rico Deal*, N.Y. TIMES, Oct. 28, 2017, at A13.

154. *Id.*

to a company with little experience of work on such a scale.[155] Furthermore, under the contract, PREPA agreed to pay electrical lineman workers $319 per hour; the average salary in Puerto Rico for such work is $19 per hour.[156]

On October 29, 2017, the Governor of Puerto Rico, Ricardo A. Rosselló, asked the governing board of PREPA to immediately cancel its contract with Whitefish Energy.[157] The Governor expressed significant concerns about how Whitefish obtained the contract, stating "the contract had become a 'distraction' and that attention had to be refocused on restoring service."[158] The Governor's statement came two days after the Federal Emergency Management Agency ("FEMA") warned that it might refuse to cover any costs if the contract between Whitefish and PREPA was found to be improper.[159]

PREPA's CEO, Ricardo Ramos, gave various contradicting explanations for his decision to choose Whitefish over mutual aid agreements with other utility companies, which are customary after disaster.[160] For example, Mr. Ramos stated that

> he preferred Whitefish because he expected the United States Army Corps of Engineers to pay the company, which meant the bankrupt utility would not have to front any of the money for repairs. Under mutual aid agreements, [PREPA] would have to pay for the work and then seek reimbursement from the Federal Emergency Management Agency.[161]

Later, however, Ramos told legislators "he went with the private company because he did not have the resources to find lodging for workers borrowed from other utilities" although "emails released [in November] by the House Committee on Natural Resources show that Whitefish workers could not find housing, either."[162] Furthermore, although Ramos has contended that he has not received any kickbacks for this contract, he acknowledged that "the company had long been rife with political patronage, and that up to half of the employees were the family members of politicians."[163] Following this widespread criticism,

155. *Id.*

156. Frances Robles, *Puerto Rico's Power Chief Steps Down in Scandal*, N.Y. TIMES, Nov. 18, 2017, at A11.

157. Frances Robles & Deborah Acosta, *Puerto Rico Cancels Contract with Small Montana Firm to Rebuild Power Grid*, N.Y. TIMES, Oct. 30, 2017, at A10.

158. *Id.*

159. *Id.*

160. Robles, *supra* note 156.

161. *Id.*

162. *Id.*

163. *Id.*

Ramos resigned on November 17, 2017.[164] About "two months after the storm, the grid is generating power at forty-five percent of capacity."[165]

Mr. Ramos's resignation highlights the lack of transparency of PREPA and that its policies have helped grow Puerto Rico's staggering amount of debt.[166] An example of the power authority's complex and paradoxical role in the economy in Puerto Rico is PREPA's free electrical power setup.[167] The power authority provides free power to government-owned enterprises, many for-profit businesses, and all of Puerto Rico's seventy-eight municipalities.[168] In exchange for free electricity, PREPA pays no property taxes or licensing fees for various cities.[169] Supporters believe the free electricity arrangement is "so tightly woven into the fabric of society that unwinding it would have vast ramifications and, some say, only worsen the plight of the people who live [there]."[170] Eduardo Bhatia, the President of the Puerto Rico Senate remarked, "If the towns don't get free energy, they're going to have to pay for it by increasing their property taxes or something, so the people will end up paying."[171] In 2014, analysts found that cities throughout Puerto Rico "had received $420 million worth of free electricity that they should have paid for."[172] Furthermore, "288 governmental bodies on the Island were delinquent in their power payments by $300 million."[173]

2. Federal Aid

On September 21, 2017, FEMA announced that federal disaster assistance has been made available to Puerto Rico to supplement the

164. *Id.*

165. Frances Robles, *C.E.O. of Puerto Rico Power Authority Resigns*, N.Y. TIMES (Nov. 17, 2017), https://www.nytimes.com/2017/11/17/us/prepa-ceo-resigns-puerto-rico.html.

166. *See* Robles, *supra* note 156.

167. *See* Mary Williams Walsh, *How Free Electricity Helped Dig $9 Billion Hole in Puerto Rico*, N.Y. TIMES, Feb. 2, 2016, at A1.

168. *Id.* at B4. The concept of free electricity dates back to 1941 when the utility company was first established by Rexford Tugwell, a member of Franklin D. Roosevelt's brain trust. *Id.* Tugwell "contended that for electricity to benefit the people, it had to be owned by the people, and he created [PREPA] by nationalizing the handful of private electric companies then on the island." *Id.* The free electricity was intended to make up for lost tax revenue in that "the value of free power was supposed to match the forgone taxes, and if the city took more, they were supposed to pay for it." *Id.*

169. Robles, *supra* note 156.

170. *See* Walsh, *supra* note 167, at B4.

171. *Id.*

172. *Id.*

173. *Id.* Among the governmental bodies delinquent in payments included public schools, hospitals, low-income housing projects, a commuter train, the Island's water and sewage system, and its highway authority, which operates traffic signals, toll plazas, and highway lighting. *Id.*

recovery efforts affected by the hurricane.[174] The federal funding is available to affected individuals in specific cities, eligible local governments, and certain private nonprofit organizations on a cost-sharing basis for emergency work in all seventy-eight municipalities.[175] On October 11, 2017, the House of Representatives voted to approve spending of $36.5 billion in disaster aid for Puerto Rico in a new package of funds that also included money to combat the wildfires on the West Coast of the mainland United States.[176] Furthermore, the governments of Puerto Rico and the Virgin Islands would have access to $4.9 billion in special loans that will allow them to continue to pay employees and vendors.[177]

Beyond the disruption of the immediate aftermath of the storm, the potential long-term repercussions may be somewhat mixed, however.[178] On one hand, a massive exodus of Puerto Ricans choosing to relocate to the United States, rather than rebuilding on the Island, will further erode Puerto Rico's economic base that had already been readily declining.[179] "On the other, an infusion of federal funds could spur the economic growth and development of infrastructure" that has otherwise eluded the Island.[180] Given the lack of taxes collected by the Puerto Rican government, major infrastructure projects, including the outdated electrical grid, have been put off.[181] The infusion of new funds will provide for major infrastructure renovations that the Island has never been able to accomplish on its own.[182] For example, energy experts have stated that the rebuilding effort "offers a unique opportunity to outfit the Island with the electric grid of the future: a state-of-the-art

174. Press Release, FEMA, President Donald J. Trump Approves Major Disaster Declaration for Puerto Rico (Sept. 21, 2017), https://www.fema.gov/news-release/2017/09/21/president-donald-j-trump-approves-major-disaster-declaration-puerto-rico.

175. *Id.*

176. Mike DeBonis, *House Approves $36 Billion in Disaster Aid, Responding to Wildfires and Puerto Rico Crisis*, WASH. POST (Oct. 12, 2017), https://www.washingtonpost.com/news/powerpost/wp/2017/10/12/house-approves-36-billion-in-disaster-aid-responding-to-wildfires-and-puerto-rico-crisis/?utm_term=.25e71714c006.

177. *Id.*

178. *Rating Action: Moody's Downgrades Puerto Rico GOs, COFINA and Other Debt After Hurricane Maria; Outlook Negative*, *supra* note 4.

179. *Id.*; *see* Patrick Gillespie, *Puerto Rico: Hurricane Maria Hammers an Economy that Can't Take Much More*, CNN: MONEY (Sept. 20, 2017, 11:38 AM), http://money.cnn.com/2017/09/20/news/economy/puerto-rico-hurricane-maria/index.html.

180. *Rating Action: Moody's Downgrades Puerto Rico GOs, COFINA and Other Debt After Hurricane Maria; Outlook Negative*, *supra* note 4.

181. Justin Worland, *Puerto Rico's Devastated Electric Grid Could Be a Big Opportunity for Renewable Energy*, TIME (Sept. 29, 2017), http://time.com/4963240/hurricane-maria-puerto-rico-electrical-grid.

182. *See id.*

system built from scratch using renewable energy sources like wind and solar, which would be cheaper to operate and would respond better to the next hurricane."[183]

On November 13, 2017, Puerto Rico's Governor appeared before the Senate and the House to ask the federal government for an additional $94 billion in disaster funds.[184] The request, however, did not include a breakdown of how the funds would be used.[185] Specifically, Mr. Rosselló requested $15 billion for health care ("without specifying what medical facilities needed to be fixed"), $8.4 billion for schools ("without noting what damages the schools had incurred") and $17.7 billion pertaining to the restoration of the power-grid.[186] Legislators, however, remain skeptical of the Island's ability and competence to handle such a massive influx of funds in light of how PREPA and the governor handled the Whitefish contract.[187] While some legislators sought answers with regard to this contract, others questioned why Puerto Rico should receive any help at all from the U.S. government when Puerto Ricans are exempt from most federal income taxes.[188] Considering the Oversight Board's lack of control to manage the funds given to the Puerto Rican government, there remain legitimate concerns as to whether leaders in Puerto Rico will be fiscally competent and transparent in their handling of the humanitarian contracts and fiscal restructuring.[189]

IV. THE ROAD TO A FISCAL RECOVERY

As Puerto Rico attempts to weather the compounding effects of the Commonwealth's fiscal and humanitarian disasters, it is unclear what shape a solution will take either through creditor negations or debt forgiveness.[190] Part of the relief may likely come in the form of a "roll-up," which is often common in major bankruptcy cases.[191] A roll-up in bankruptcy allows for a debtor struggling to obtain financing, to fund its

183. *Id.*

184. Andrés L. Córdova, *Two Months Later: Puerto Rico Doesn't Have Power, Education or Economy Running Again*, HILL (Nov. 20, 2017, 1:40 PM), http://thehill.com/opinion/energy-environment/361211-two-months-later-puerto-rico-doesnt-have-power-education-or.

185. Frances Robles, *After Utility Deal Scandal, Puerto Rico Asks for $94 Billion*, N.Y. TIMES, Nov. 15, 2017, at A11.

186. *Id.*

187. *Id.*

188. *Id.*

189. Long, *supra* note 106, at 80.

190. Mary Williams Walsh, *Lenders Offer Some Help in Turning Lights Back On*, N.Y. TIMES, Sept. 28, 2017, at A20.

191. *Id.*

operations by asking pre-petition lenders to inject money into the estate by offering a post-petition facility that effectively pays off or "rolls-up" a pre-petition debt.[192] In exchange, the pre-petition lender will provide a new loan to the debtor.[193] The new roll-up loan is given an upgraded priority status by transforming the existing lenders' pre-petition claims into a post-petition administrative expense; a status that has preferential treatment on the priority totem pole.[194] The rationale behind a roll-up is that when a debtor has no other reasonable prospect of financing its business operations, the lender would have a better chance of getting repaid if the debtor is able to continue its business rather than if the debtor was forced to cease operations.[195] In Puerto Rico, for example, a group of bondholders that includes mutual and hedge funds have offered to lend Puerto Rico "$1 billion to pay for urgent repairs and to cancel $150 million of the power company's outstanding debt in the process."[196] The bondholder's loan would take priority over some of Puerto Rico's other debts and would offset some losses the bondholders may face if the original debt is not paid in full.[197] As such,

> [u]nder the terms of the $1 billion loan being offered by bondholders, Puerto Rico would not have to make principal or interest payments for two years. During that time, the interest would accumulate at a variable rate starting at about five and a half percent and following market rates up or down.[198]

The $150 million roll-up would exchange $1 billion of outstanding defaulted bonds for new, viable bonds with a face value of $850 million.[199]

Others have called upon the federal government to wipe out the debt completely.[200] In a statement to Fox News, President Trump hinted that Puerto Rico's crippling debt ought to be forgiven.[201] White House budget director Mick Mulvaney has since dialed back the President's

192. David Griffiths, *Roll-up, Roll-up, Read All About It!*, WEIL BANKR. BLOG (Oct. 6, 2010), https://business-finance-restructuring.weil.com/dip-financing/roll-up-roll-up-read-all-about-it.

193. *Id.*

194. *Id.*

195. *Id.*

196. Walsh, *supra* note 190.

197. *Id.*

198. *Id.*

199. *Id.*

200. Nathan Bomey, *6 Reasons Why Puerto Rico Slid into Financial Crisis*, USA TODAY, https://www.usatoday.com/story/money/2017/10/04/puerto-rico-debt-crisis-bankruptcy-donald-trump/731091001 (last updated Oct. 4, 2017).

201. Victor Morton, *Puerto Rico's $70 Billion Debt Will Have to Be Wiped out, Trump Says*, WASH. TIMES (Oct. 3, 2017), http://www.washingtontimes.com/news/2017/oct/3/puerto-ricos-debt-will-have-be-wiped-out-trump-say.

statement and stated that Trump's comments should not be taken literally.[202] Still, many believe that a total debt forgiveness for Puerto Rico may be a viable alternative to the debt restructuring in light of the destruction wreaked by Hurricane Maria.[203] As previously mentioned, prior to the storm, the Oversight Board developed a plan to wipe out seventy-nine percent of the annual debt payments.[204] Since Hurricane Maria's landing on Puerto Rico, the prices of bonds have dropped dramatically.[205] Some believe that this drop in bond prices may ultimately help Puerto Rico's path out of bankruptcy.[206] Following this drop in prices, "investors have unloaded the Island's bonds at the fastest pace in three years, pushing prices to one new low after another."[207]

Still, an elimination of debt will not solve the longstanding economic instability and dependence that has forced Puerto Rico into this economic predicament in the first place.[208] Puerto Rico must focus on a solution that affords the Commonwealth long-term fiscal stability and enables the Island's economic independence.[209] Rather than depending on tax breaks to attract foreign corporations, Puerto Rico's relief strategy should focus on growing local businesses, universities, and infrastructure.[210] Subpart A discusses how Congress should alter PROMESA to give the Oversight Board more authority to supervise the control regarding the fiscal management of the Island and the ongoing humanitarian relief.[211] Following these amendments, Subpart B discusses how relief should be grounded in long-term initiatives that construct an autonomous economy.[212] By focusing on initiatives, which promote the health of its insular and local economy, Puerto Rico may be able to relieve itself of the codependency that has historically plagued the Island.[213]

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202. Justin Sink & Jennifer Epstein, *No U.S. Bailout for Puerto Rican Debt, Trump's Budget Chief Says*, BLOOMBERG POL., https://www.bloomberg.com/news/articles/2017-10-04/trump-suggests-puerto-rico-s-debt-may-need-to-be-wiped-out (last updated Oct. 4, 2017).

203. Kate Aronoff, *Puerto Rico Is on Track for Historic Debt Forgiveness—Unless Wall Street Gets Its Way*, INTERCEPT (Oct. 4, 2017, 2:02 PM), https://theintercept.com/2017/10/04/puerto-rico-debt-forgiveness-hurricane-maria.

204. *Id.*

205. Michelle Kaske, *Puerto Rico Bond-Trading Blitz Could Ease Path from Bankruptcy*, BLOOMBERG (Nov. 16, 2017, 11:04 AM), https://www.bloomberg.com/news/articles/2017-11-16/puerto-rico-bond-trading-blitz-seen-easing-path-from-bankruptcy.

206. *Id.*

207. *Id.*

208. Allen & Peñaloza, *supra* note 60.

209. *See infra* Part IV.

210. *See infra* Part IV.B.

211. *See infra* Part IV.A.

212. *See infra* Part IV.B.

213. *See infra* Part IV.

A. Amendments to PROMESA to Give the Oversight Board Supervisory Powers

Some critics believe that PROMESA is hampering more than helping the storm recovery efforts, leading some to call for amendments to the legislation.[214] While PROMESA places Puerto Rico under the Oversight Board and subjects its debt to a court-supervised restructuring, the legislation greatly limits the authority that the bankruptcy judges and other federal officials can exert over the insolvent local governments.[215] After the public outcry regarding PREPA's Whitefish contract, many called upon the Oversight Board to cancel the contract and remove the PREPA CEO.[216] However, after hearing such arguments from bondholders, Judge Laura Taylor Swain ruled that the Oversight Board had no legal authority to install new leadership at the power company.[217] Furthermore, Judge Swain added that the Board had no authority to impose austerity measures on Puerto Rico, even if it thought steps taken by Governor Ricardo Rosselló did not go far enough.[218] While many Puerto Ricans blamed the Governor for failing to fix the electrical grid and awarding the contract to Whitefish, the Governor appeared emboldened by Judge Swain's restriction of the Oversight Board and attested that the Oversight Board had authority in just three areas: representing Puerto Rico in the restructuring proceedings; ensuring that its budget is balanced; and helping the Island regain its ability to tap the public credit markets.[219]

Although Congress may tie specific strings to the money it affords Puerto Rico, many believe that the undercurrent of corruption and inefficiency of Puerto Rican politicians is what created the fiscal crisis in the first place.[220] Particularly in light of the questionable contracting practices of PREPA, PROMESA should be amended in order to

214. Mary Williams Walsh, *Crisis Law Snags Puerto Rico Recovery*, N.Y. TIMES, Nov. 17, 2017, at B1, B5.

215. *Id.*

216. *Id.*

217. *Id.*

218. *Id.*

219. *Id.*

220. *Id.* Puerto Rico has a historical practice of misrepresenting its financial condition whether by falsifying documents or failing to provide accurate budget numbers. Long, *supra* note 106, at 80. The Island's government has routinely been unable or unwilling to provide Congress with accurate numbers that explain the Island's financial needs and this lack of transparency has only exacerbated the Island's financial woes. Mary Williams Walsh, *A Hurdle to Transparency*, N.Y. TIMES, Nov. 5, 2015, at B1, B4.

strengthen the Oversight Board's authority and congressional oversight in the recovery process.[221] Accordingly, the Oversight Board should be tasked with more fiduciary and administrative control over the money, such as in the situation with PREPA.[222] While the Oversight Board has some budgetary and financial control, and approval of key energy and "critical projects," the role of the Board in practicality, is substantially limited.[223] One way to implement more control to the Oversight Board, without risking Puerto Rico's internal sovereignty, would be to appoint more elected officials to the Board.[224] By including the Governor of Puerto Rico, the heads of major agencies, and other representatives, the Oversight Board would consist of both representatives and experts who would be able to provide the officials with the knowledge and experience necessary to provide competent advice regarding the long-term plans of Puerto Rico.[225] After adding specific legislators and government representatives, the Oversight Board should be allotted the authority to approve or reject the signing of contracts, the ability to impose austerity measures, and remove government appointees for cause.[226] Tasking the Oversight Board with more responsibility would provide a transparent mechanism that can make sure that Puerto Rico is utilizing U.S. funds in the best interest of all Puerto Ricans and crafting a legitimate and realistic plan for the future economic standing of Puerto Rico.[227]

The concept of granting the Oversight Board with more authority may be likened to the financial troubles experienced by Washington, D.C. in the 1990s.[228] On April 7, 1995, Congress approved legislation to create a financial control board for the District of Columbia.[229] The five-member financial control board was appointed by President Clinton and was granted vast authority over municipal spending, financial planning,

221. Andrés L. Córdova, *We Need to Reevaluate Puerto Rico's Territory Status as We Rebuild*, HILL (Nov. 7, 2017, 12:20 PM), http://thehill.com/opinion/energy-environment/359109-we-need-to-reevaluate-puerto-ricos-territory-status-as-we-rebuild.

222. *See* Walsh, *supra* note 214, at B5.

223. *Id.*

224. *Id.*

225. *Id.*

226. *Id.*

227. *See A Hurdle to Transparency*, *supra* note 220.

228. AUSTIN, *supra* note 105, at 3; Michael Janofsky, *Congress Creates Board to Oversee Washington, D.C.*, N.Y. TIMES (Apr. 8, 1995), http://www.nytimes.com/1995/04/08/us/congress-creates-board-to-oversee-washington-dc.html.

229. Janofsky, *supra* note 228.

borrowing, hiring, and contracts.[230] Similar to the Oversight Board in Puerto Rico, the control board was tasked with

> ensur[ing] that the District efficiently and effectively deliver services to its residents; enhance the District's timely payments of its debts; increase the city's access to capital markets; assure the city's long-term economic vitality and operational efficiency; and repair and foster a better relationship between the District and the Federal Government.[231]

However, to ensure such goals were achieved, Congress vested the control board with broad powers traditionally reserved for the city government.[232] These powers included the authority to approve or reject the city's annual budget, its financial plan, and any attempts to spend or borrow in the city's name, and to review all future and existing contracts.[233] Furthermore, all District spending was to be routed through the control board.[234] The board also was expected to approve the Mayor's appointments to key government positions, including the Chief Financial Officer, have the authority to remove such appointees for cause, and, in extraordinary circumstances, disapprove of District laws passed by the City Council.[235] Following the implementation of this law, the District of Columbia's fiscal health vastly improved as the economic improvements resulted in a balanced budget, investment-grade credit rating, and a larger economy.[236]

The situation plaguing Puerto Rico is similar to that faced by Washington, D.C. in that its "hybrid municipal entity" impacted its long term financial viability because while "it lacked revenue support from a state government," it "was forced by necessity to provide its residents services normally funded by a state."[237] By affording the Oversight Board similar control, the Board will be able to implement long-term practices to encourage fiscal discipline.[238] After affording the Board such responsibility, the Board should look to restrain spending, control expenditures through budget management tools, and improve revenue collection, capacity, and estimation.[239] Furthermore, by allowing the

230. *Id.*
231. DC APPLESEED & OUR NATION'S CAPITAL, BUILDING THE BEST CAPITAL CITY IN THE WORLD 82 (2008) [hereinafter BUILDING THE BEST CAPITAL CITY IN THE WORLD].
232. *Id.*
233. *Id.*
234. *Id.*
235. *Id.*
236. *Id.* at 107.
237. *Id.* at 83-85.
238. *See id.* at 83-85, 107.
239. *See id.* at 113-15.

Board the power to approve contracts, the Board will be able to ensure that similar problems to the Whitefish Energy contract do not occur again.[240]

B. Amendments to Puerto Rico's Constitution

Puerto Rico's financial troubles are symptomatic of irresponsible budgeting, issuing bonds beyond the debt ceilings, and oppressive spending.[241] Puerto Rico's economy has historically been focused on tax schemes, like those that expired in 2006, which promote artificial stability.[242] Following the Congressional amendments to PROMESA, Puerto Rico and the Oversight Board should: (1) amend the Puerto Rican Constitution to include a debt ceiling that limits the debt capacity to Puerto Rico's total revenue rather than "total resources"; (2) enhance tax collection problems through increased efficiency systems; and (3) implement new tax incentives that will spur local business growth in companion with initiatives dedicated towards foreign corporate development.[243] The combination of these initiatives will provide a framework that can incentivize responsible long-term planning based on realistic projections.[244] Incentivizing local businesses will encourage Puerto Rican workers to enter the workforce, which will grow the economic base.[245] Encouraging local business growth will in turn generate more revenue through sales and income taxes.[246] When the collection of such taxes are properly accounted for, the Puerto Rican government will be afforded a better picture of the actual revenue generated, which will provide a better picture for the amount of debt the government can issue.[247] When the Oversight Board is given direct supervisory powers over the financial affairs of its municipalities with respect to the budget, revenue calculation, and cash management, Puerto Ricans, U.S. representatives, and bondholders can have the

240. *See* Walsh, *supra* note 214, at B5.

241. *See supra* Part II.

242. Greenberg & Ekins, *supra* note 25.

243. JOFFE & MARTINEZ, *supra* note 41, at 10; *see* BUILDING THE BEST CAPITAL CITY IN THE WORLD *supra* note 231, at 114-15; Cate Long, *Decades of Debt: The Puerto Rico Fiscal Crisis*, CITY & SLATE (Oct. 22, 2015), http://cityandstateny.com/articles/somos/road-to-somas-coverage/decades-of-debt-the-puerto-rico-fiscal-crisis.html.

244. *See* BUILDING THE BEST CAPITAL CITY IN THE WORLD, *supra* note 231, at 115-16.

245. *Id.*

246. *Id.*

247. *Id.*

assurance that government functions are being administered with the requisite transparency and competency necessary to run a functioning government.[248]

Additionally, while foreign corporate tax initiatives are important, tax incentives should focus on the growth of Puerto Rico's economy, independent of foreign corporations.[249] Although most of Puerto Rico's current tax incentives can be used by local companies, many of the incentives were designed to entice outside corporations to do business in Puerto Rico.[250] Practically, local startups cannot take advantage of the incentives because they require the company to have ongoing taxable revenue.[251] Instead, incentives should focus on encouraging entrepreneurial spirit whether by building infrastructure or encouraging enrollment in local universities.[252] A way of encouraging business growth of foreign corporations, while also growing Puerto Rico's insular economy, could be to identify specific services that big companies may look to outsource from Puerto Rico.[253]

V. CONCLUSION

There is no easy solution for Puerto Rico.[254] Instead, Puerto Rico's path toward sovereign solvency will be lengthy, complex, and require various changes to practices that the government has historically rested upon.[255] Because its debt crisis derives from a multitude of sources, Puerto Rico is in need of viable long-term solutions that can reshape the various practices and loopholes that have resulted in the rapid accumulation of debt.[256] While decades of questionable governmental procedures may have encouraged the overwhelming municipal debt, Hurricane Maria further upended the Island's delicate future financial plan.[257]

248. *See* Long, *supra* note 243.
249. *See* Brown, *supra* note 30.
250. *Id.*
251. *Id.*
252. *Id.*
253. *Id.*
254. *See* Long, *supra* note 243.
255. *Id.*
256. *Id.*
257. *See* Long, *supra* note 106, at 80; Walsh, *supra* note 220, at B4.

The devastation left behind by Hurricane Maria has created a new reality for Puerto Rican municipalities and creditors in which they must reconcile the parallel economic and humanitarian disasters.[258] Although significant amounts of federal aid and private insurance proceeds will be available to help rebuild Puerto Rico's shattered infrastructure, it is unlikely that the Commonwealth will be able to cover any shortfalls.[259] The ongoing crisis in Puerto Rico may have serious repercussions if the Title III restructuring proceedings do not succeed in relieving the Commonwealth's crushing debt and providing a realistic fiscal roadmap for the years to come.[260] Given the significance of U.S. based investor funds in Puerto Rico's debt, a restructuring failure will have reverberating effects on the U.S. economy, as well as Puerto Rico's ability to rebuild after the crushing effects of Hurricane Maria.[261]

In order to escape the financial and humanitarian crises plaguing the Island, Puerto Rico must alter the status quo that encouraged unreasonable spending and irresponsible budgeting.[262] Puerto Rico must leverage this opportunity to restructure its debts under PROMESA to form long standing solutions that will allow its economy to thrive independent of corporate entities.[263] Furthermore, by affording the Oversight Board strong and independent control over the Island's finances, similar to Washington, D.C., Puerto Rico may be able to regain control of its bloated budget and get its fiscal affairs back on track.[264]

Fortunately, Puerto Rico has a culture of resilience.[265] Puerto Rican citizens continue to remain steadfast as they face the daunting tasks of rebuilding their homes, businesses, and livelihoods.[266] No matter the path that a long-term financial solution will take, it can be sure that "Puerto Rico will not only survive this. It will bloom once again."[267] In the words of Justice Sonia Sotomayor, "[W]e are united in the firm belief that Puerto Rico will persevere. The incredible spirit and strength of the Puerto Rican people is unbreakable. Our island has faced

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258. Nick Brown, *Hurricane Changes the Game for Puerto Rico Bond Investors*, REUTERS (Nov. 21, 2017, 5:16 PM), https://www.reuters.com/article/us-usa-puertorico-restructuring/hurricane-changes-the-game-for-puerto-rico-bond-investors-idUSKBN1DL2SN.

259. *See* Worland, *supra* note 181.

260. *See* Schutlz, *supra* note 123.

261. *Id.*

262. Long, *supra* note 106, at 80.

263. *See* Brown, *supra* note 30.

264. BUILDING THE BEST CAPITAL CITY IN THE WORLD, *supra* note 231, at 114-15.

265. *See* Holmes, *supra* note 5.

266. Lluveras, *supra* note 1.

267. *Id.*; *see* Cristian Farias, *Sonia Sotomayor's Message of Hope to Puerto Rico: 'You Are Not Alone'*, N.Y. MAG. (Sept. 27, 2017, 9:48 AM), http://nymag.com/daily/intelligencer/2017/09/sonia-sotomayors-message-of-hope-to-puerto-rico.html.

innumerable challenges throughout the centuries. However, each and every time, Puerto Rico has emerged stronger. And we will do so again."[268]

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268. Farias, *supra* note 267.

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