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Pierluisi Equates Federal Fiscal Control Board to Colonialism

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WASHINGTON — Puerto Rico's congressional representative Pedro Pierluisi strongly opposed the idea of the federal government imposing a federal fiscal control board on Puerto Rico, warning it would be "a blatant exercise of colonialism."

The Democrat, a nonvoting member of Congress, made his comments on Tuesday at a policy forum on Puerto Rico sponsored by The Hill. He added that anyone who proposes a federal control board would also draw opposition from Puerto Rico residents and "anybody who believes in democracy in the world."

Gov. Alejandro García Padilla also opposes a federal control board.

"I'm the first one who says if you want to do additional oversight in exchange for additional funding, or something like Chapter 9 [bankruptcy protection], I'm fine with it," Pierluisi said. "But this is not so easy as saying let's impose a fiscal control board on Puerto Rico."

Pierluisi's comments respond to suggestions from some Republican lawmakers that a federal control board would have to be created before Congress helps the island with its fiscal crisis and roughly $72 billion of debt.

Members of Congress have floated multiple options, with Pierluisi introducing a bill in February that would extend Chapter 9 bankruptcy protections to the island's public authorities. The Chapter 9 solution has gained traction among Democrats, but has fallen flat with Republicans.

The discussion about federal fiscal oversight at Tuesday's forum partially stemmed from questions about a four-part proposal the Treasury Department recently released to help Puerto Rico. The plan calls for extending Chapter 9 to all of Puerto Rico, instituting federal fiscal oversight on the island, and providing increased federal healthcare and tax credits that are currently unavailable to Puerto Ricans living on the island.

Pierluisi said he disagrees with Treasury that the commonwealth needs access to an all-encompassing form of Chapter 9 and that a bankruptcy regime that extends to public authorities is enough to let Puerto Rico handle its debt. Bankruptcy only for public authorities would still require Puerto Rico to get its fiscal house in order and promote growth, he said.

Jeffrey Farrow, chairman of the Oliver Group and an advisor to Akin Gump & ACG Analytics, agreed during a separate panel that the Treasury's bankruptcy and oversight proposals are flawed. He said officials and experts "should not even be talking about a control board as an option" and pointed out that if Pierluisi's bill has gained no traction in the Republican-controlled Congress, officials should "question the viability of going beyond that."

But Arturo Porzecanski, a professor and distinguished economist in residence at American University's School of International Service, said Puerto Rico Gov. Alejandro Garcia Padilla "wants to have his cake and eat it too."

"Under local law and the local constitution, he is supposed to pay his debts," Porzecanski said. "So he wants the federal government to get Congress to overwrite the [local] Constitution and local law and give him a free pass not to comply with the bond indentures." At the same time, the governor is saying 'don't mess with my independence,' Porzecanski said.

Pierluisi proposed Congress could add his bankruptcy bill or extend the Earned Income Tax Credit to Puerto Rico in its upcoming omnibus spending bill, which must be enacted by Dec. 11.

But given the lack of movement in Congress, Mark Calabria, the director of financial regulation studies for The Cato Institute, said during a third panel that there are administrative steps the Treasury Department and Federal Reserve Board could take to help Puerto Rico, but they would pose major challenges and could be politically risky.

Calabria said Section 14 of the Federal Reserve Act was not designed to be an assistance program, but allows the Fed to invest in state or municipal debt from the continental United States. The act defines continental United States as any state or the District of Columbia, but Calabria said there is an argument, although quite thin, that could be made for Puerto Rico to be included. The section is designed to be used as a small fix, not a structural reform, and also requires the investments to be in maturities of less than six months and in debt that is payable. Those restrictions pose significant hurdles for Puerto Rico, Calabria said.

Section 13, which was used during the financial crisis for AIG and Bear Stearns, may be an easier way to go, although it still poses challenges, he said. Under this section, the Fed could buy debt from public corporations on the island but not Puerto Rico's government. The Fed would also have to show that the entities are not insolvent and be broadly applicable to all the corporations, not just ones heavily in need.

Finally, the Treasury could use its Exchange Stabilization Fund to address the situation. The option, which is generally structured to provide liquidity, has the most flexibility of any the three potential solutions, but there is "certainly some political risk" with the idea, Calabria said. If it were to be implemented, it would require a commitment from Treasury Secretary Jack Lew and, at least implicitly, backing from President Obama.