Wall Street demands austerity in Puerto Rico

By John Marion
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The ongoing attack on US municipalities and states that has resulted in the bankruptcy of Detroit is spreading, and predatory lenders have set their eyes on Puerto Rico. The US commonwealth—a colony seized from Spain in 1898—is home to about 3.7 million people and has $US 70 billion in debt. Profits on its bonds are tax free in every US state and have therefore been bought widely.

The ruling establishment has launched a two-pronged assault, through undemocratic scheming among lenders and austerity measures which include raising the retirement age for teachers. As has become commonplace, the island's economic recession—which predates the 2008 world crash—is being blamed on workers and their pensions.

The bourgeois press, including the *Wall Street Journal*'s Market Watch, write openly that Puerto Rico is to be treated like Detroit. Notwithstanding the fact that Puerto Rico, like US states, cannot go bankrupt, a default on its bonds would be disastrous for capitalism.

A chart in the Janney Capital Markets "Puerto Rico: Accomplishments and Challenges" report of September 2013 shows a drastic jump in yields on the commonwealth's bonds after Barron's published an article expressing concerns about default. Bond prices also dropped sharply after the Puerto Rican Supreme Court's recent decision to stay the implementation of pension cuts.

As in Detroit, austerity measures will be enforced by fiat if necessary. On January 7, globalpost.com reported that "an overhaul of the teachers' pension system was demanded by ratings agencies who are threatening to downgrade Puerto Rican government bonds to junk status."

Austerity is being enforced by Governor Alejandro García Padilla of the Partido Popular Democratico (PPD), who was elected in November 2012. The PPD, a defender of the island's commonwealth status against independence or statehood, was instrumental in enforcing that

status during the 1940s through the infamous Gag Law, which carried a ten year prison sentence for singing, speaking, or writing in favor of Puerto Rican independence.

García Padilla, also a member of the US Democratic Party, has increased the borrowing authority of the Sales Tax Financing Authority,—known by its Spanish acronym COFINA— along with the amount of money it receives from Puerto Rico's sales and use tax. In an indication of things to come, García Padilla promised in his inaugural address to "assure that universal access to health services with cost-efficiency is no longer a contradiction in terms."

The manner in which COFINA is supported by sales and use tax revenues is vampiric. An October 4, 2013 report by Janney Capital Markets described the process: each year COFINA sucks up sales tax revenues until that year's Pledged Sales Tax Base Amount is reached. In 2010 that amount was approximately $550 million. Even when the Base Amount has been reached, additional sales tax revenues are split between COFINA and the Puerto Rican treasury. García Padilla has sought to increase COFINA's portion of this latter amount as well.

In Puerto Rico's 2013 fiscal year, which ended June 30, its total debt service cost $607 million, or nearly half of the total $1.17 billion of sales tax revenues.

While the rich profit from lending, staggering numbers of Puerto Ricans live in poverty. In 2009 more than 41 percent of the population lived below the official poverty level, which is lower than that for the US mainland. According to the US Census Bureau, the median household income in 2012 was $19,429.

Even under these conditions, capitalism is not satisfied with its profits: an analyst from the Cato Institute recently complained to Fox News Latino that corporations in Puerto Rico are "bound by U.S.-mainland minimum wage laws."

In a law passed on Christmas Eve, the minimum retirement age for public school teachers was increased to 62 for new employees and 60 for many existing employees who had been promised an earlier retirement. Mandatory teacher contributions to the pension plan were also increased from 9 to 10 percent. Janney estimates that these "reforms" will cut the government's pension expenses by $700 million per year over the next 25 years.

Conditions for other workers are also under attack. A presentation by government officials to the 2012 Puerto Rico Credit Conference boasted that government payroll expenses had been cut by 1/3 since 2009.

The state-run monopoly PRASA (Puerto Rico Aqueduct and Sewer Authority) is increasing water and sewer rates by 60 percent. A tripling of the excise tax on petroleum to fund PRHTA (the Puerto Rico Highway and Transit Authority) will force workers to ration their use of gasoline.

The austerity measures resulted in a two-day strike by the island's school teachers last week. Only 12 percent of public school teachers went to work on January 14, and fewer than 200 students out of an island-wide total of 425,000 went to school, according to ABC News. The

Associated Press quoted a 43-year-old history teacher from the Santurce district of San Juan: "'They're condemning us to retirement in poverty.'"

Nonetheless, the strike was quickly diverted by the unions into safe channels. The AP article continued: "… following hours of protest, union leaders and government officials announced the creation of a committee to study alternatives to a law approved on Christmas Eve that calls for switching from a defined benefit plan to a defined contribution system, among other changes."

Puerto Rico has been in recession for much of the last eight years and the corporate press has used this fact cynically, claiming that the recession is caused by welfare programs and overly generous benefits for workers.

In reality, many factors have fed into the recession: the island's reliance on imports, its lack of natural resources, US restrictions on its options for shipping exports, US federal tax law, and in the last 20 years, competition from cheaper labor in Latin American countries that signed onto NAFTA.

For many years, US companies received large tax breaks on their Puerto Rican operations through Section 936 of the IRS code. Significant numbers of pharmaceutical, banking, and electronics manufacturing jobs resulted. In 1993, the *New York Times* reported that "Nearly 60 percent of tax benefits—estimated at $2.7 billion a year—go to some 60 drug companies that account for 18 percent of the jobs provided by Section 936." Even at that point, unemployment was at 18 percent, and the benefit was just for corporate profit.

Section 936 was repealed in 1996, but a 10-year grace period was implemented through a modified law called Section 30A, which allowed significant deductions from corporate taxes. That US law expired in 2006. Even with the expiration of Section 30A, American corporations pay a paltry amount of taxes on Puerto Rico. The web site of the Chamber of Commerce boasts that the maximum corporate tax rate will be reduced from 30 percent to 25 percent in 2014, and that in some sectors it is already lower than 5 percent.

Behind-the-scenes scheming to impose austerity has taken two forms. In the first, a "US advisory team" was convened at the beginning of December, according to Fox News Latino. Representatives from the US Departments of Education, Health and Human Services (HHS), Housing and Urban Development (HUD), and Environmental Protection Agency (EPA) are involved. The team's job is to "maximize federal funds" use without providing any additional money; in other words, it will impose austerity measures. A high-ranking member of the opposition Partido Nuevo Progresista compared it to receivership.

The second is a seminar held on January 16 in New York and sponsored by Jones Day, the law firm spearheading Detroit's bankruptcy. The Puerto Rican government was not involved in the seminar, but investors' arrogance was expressed in a January 17 Fox News Latino column written by Justin Vélez-Hagan, the Executive Director of the National Puerto Rican Chamber of Commerce. He began the column by gloating that "Puerto Rico's creditors, holding a meeting in New York Thursday to discuss their fears of an inevitable debt default, had this message for the island's administrators: you're not invited."

Referring obliquely to Puerto Rico's elected government as "fiscal administrators" and management, Vélez-Hagan continued that the commonwealth's creditors "met with debt restructuring specialists to consider how to handle the increasing likelihood that Puerto Rico will not be able to keep up with its payments. The fact that fiscal administrators weren't invited to defend themselves might also suggest that lenders have lost confidence in management."