Memo for the Movement

Sensible Reform

For The People of Puerto Rico

May 23, 2016
Washington, DC

Puerto Rico is broke. That means it can’t pay its debts. But the majority of the debt is owed not by the Commonwealth of Puerto Rico but by public corporations and specific government authorities.

Puerto Rico is not, yet, bankrupt. Being bankrupt means that a person or entity has been through a legal bankruptcy proceeding. But the U. S. bankruptcy code does not allow U. S. Territories to do the same.

There is now, and there will be more, pressure on Congress both to pass legislation allowing Puerto Rico to file for bankruptcy, and to go a step further and actually bail out Puerto Rico and its public corporations. Both steps are bad policy and both should be avoided.

People, companies, states, and territories don’t just “go” broke. Willful prior activity is required.

The danger of a direct taxpayer bailout to the public at large is obvious: it takes funds from the people who are both prudent and who gained nothing from any dealings with the debtor (i.e., the taxpayers) and gives the funds to the imprudent who did profit from dealing with the debtor (in this case, the people and institutions that lent money to Puerto Rico), while at the same time sending a message to other potential lenders that prudence is for losers — that the willful, prior activity of lending to people or institutions that are bad credit risks, and making a profit on those loans, will not result in financial loss.

Puerto Rico has a long history of financial mismanagement brought about by progressive politics and crony capitalism. The private sector has been routinely stifled for decades and workers receive a lower share of income than in any of the fifty states.
Progressive politicians, who are already seeking an indirect bailout – in the form of upending the existing legal structure to allow bankruptcy -- in the U.S. Congress, argue that a bailout or bankruptcy will help the people of Puerto Rico. It will not, nor would a direct taxpayer bailout. What will help the people of Puerto Rico (as differentiated from the crony capitalist lenders) is the application, voluntary or otherwise, of rules and procedures that promote sensible free market activity and democratic accountability.

Sensible economic reforms include allowing Puerto Rico (1) to set its own minimum wage law, including not having a minimum wage law; (2) to be exempt from U.S. overtime rules (which have just been greatly expanded by presidential fiat); and (3) to be exempt from the Jones Act, a protectionist measure that regulates U.S. shipping practices.

Puerto Rico should also be required to make more accurate and uniform pension disclosure a condition of receiving preferential tax treatment for all municipal bonds so that potential investors can know the true liabilities.

In addition, Puerto Rico’s legislature should be instructed to enact some simple reforms: make available audited current financial statements; end privileges that allow some customers free access to public utilities; and enact a civil service law and reduce the number of political appointments to a few hundred.

Sensible reforms do not include several proposals currently being floated, including: (1) a proposal to further increase transfer payments to Puerto Rico, which Congress did last year in the omnibus; and (2) the creation of a narrowly empowered “Oversight Board” seen as having tyrannical powers. That is a recipe for having enough power to be blamed for failure but not enough to succeed. As in any democracy, the people who make decisions should be accountable to the voters who have to live with those decisions.

Congress should not upend the existing legal system to give Puerto Rico legal protections from its creditors. Federal intervention between debtor and creditor could set a dangerous precedent for troubled state and local governments, and thus potentially disrupt the municipal bond market.

If the current debts of the public corporations and specific government authorities in Puerto Rico go unpaid, the result will be that bondholders will lose money and public utilities may go into receivership. That might result in much-needed reforms.

Puerto Rico’s public bonds were issued within specified legal frameworks. Those who bought and sold the bonds can work out the insolvencies under the rules they agreed to when they entered into the contracts. Changing the bankruptcy rules now would set a precedent for tilting the law in favor of political entities.

In the absence of a bailout or change in bankruptcy laws, Puerto Rico’s utilities would be forced to deal directly with their creditors, as the electric company PREPA has done for the past few years. Those internal reforms are often painful for insiders, but they are good for customers and they would improve the utilities’ long-term viability. It is true
that Puerto Rico may be forced to default on some debts, possibly through an agreement with its creditors. That would offer the creditors the opportunity to demand structural reforms for Puerto Rico’s economic regulation and fiscal process, without which the prospects for future repayment are dim. A bailout or change in bankruptcy laws would short-circuit this process, leaving in place the corruption, patronage, and unresponsive government that has prevented Puerto Rican incomes from catching up with those on the mainland. Default is a powerful lesson for profligate lenders.

There will undoubtedly be many more proposals for solving Puerto Rico’s financial crisis. But both citizens and legislators, in Puerto Rico and on the mainland, should remember that Puerto Rico’s crisis is not just a financial crisis: it’s a democracy crisis as well. Puerto Rico has suffered from decades of bad management — but management by legislators elected by the citizens of Puerto Rico. The people of Puerto Rico need to clean their own house if, in the future, they want and expect to live in a house that is clean.

The Honorable Edwin Meese III
Former Attorney General
President Ronald Reagan

The Honorable Becky Norton Dunlop
Chairman, Conservative Action Project
Former White House Advisor
President Ronald Reagan

William L. Walton
Vice President
Council for National Policy

The Honorable Bob McEwen
U.S. House of Representatives
Former Member, Ohio

Alfred S. Regnery
Chairman
Law Enforcement Legal Defense Fund

The Honorable J. Kenneth Blackwell
Chairman
Constitutional Congress, Inc.

General Jerry Boykin
Executive Vice President
Family Research Council

Ed Corrigan
Former Executive Director
Senate Steering Committee

Marjorie Dannenfelser
President
Susan B. Anthony List

Diana L. Banister
President
Shirley & Banister Public Affairs

The Honorable Mike Hill
Florida State Representative

Susan A. Carleson
Chairman and CEO
American Civil Rights Union

Seton Motley
President
Less Government

Floyd Brown
President
Western Center for Journalism
<table>
<thead>
<tr>
<th>Name</th>
<th>Position/Title</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rebecca Hagelin</td>
<td>Secretary, Council for National Policy, Board of Directors, FamilyTalk</td>
</tr>
<tr>
<td>Mathew D. Staver</td>
<td>Founder and Chairman, Liberty Counsel</td>
</tr>
<tr>
<td>The Honorable Belden Bell</td>
<td>Trustee, The Heritage Foundation</td>
</tr>
<tr>
<td>Kenneth F. Boehm</td>
<td>Chairman, National Legal and Policy Center</td>
</tr>
<tr>
<td>Tricia Erickson</td>
<td>President, Angel Pictures and Publicity, Inc.</td>
</tr>
<tr>
<td>The Honorable T. Kenneth Cribb, Jr.</td>
<td>Former Domestic Advisor, President Ronald Reagan</td>
</tr>
<tr>
<td>Kevin Kookogey</td>
<td>President and Founder, The Advancing Church</td>
</tr>
<tr>
<td>Richard Falknor</td>
<td>Publisher, Blue Ridge Forum</td>
</tr>
<tr>
<td>Susan Falknor</td>
<td>Publisher, Blue Ridge Forum</td>
</tr>
<tr>
<td>Gary L. Bauer</td>
<td>President, American Values</td>
</tr>
<tr>
<td>Ren O. Broekhuizen</td>
<td>Retired</td>
</tr>
<tr>
<td>George Landrith</td>
<td>President, Frontiers of Freedom</td>
</tr>
<tr>
<td>The Honorable Mike Spence</td>
<td>President, Conservative Republicans of California</td>
</tr>
<tr>
<td>C. Preston Noell III</td>
<td>President, Tradition, Family, Property, Inc.</td>
</tr>
<tr>
<td>Todd W. Herrick</td>
<td>COB, Herrick Foundation</td>
</tr>
<tr>
<td>Michael R. Long</td>
<td>State Chairman, NYS Conservative Party</td>
</tr>
<tr>
<td>Willes K. Lee</td>
<td>President, National Federation of Republican Assemblies</td>
</tr>
<tr>
<td>Allen Hebert</td>
<td>Director, American Chinese Fellowship</td>
</tr>
<tr>
<td>Richard A. Viguerie</td>
<td>Chairman, ConservativeHQ.com</td>
</tr>
<tr>
<td>Tim LeFever</td>
<td>Chairman, Capitol Resource Institute</td>
</tr>
<tr>
<td>Lee A. Beaman</td>
<td>Chief Executive Officer, Beaman Automotive</td>
</tr>
<tr>
<td>Dr. John C. Eastman</td>
<td>Henry Salvatori Professor of Law &amp; Community Service, Dale E. Fowler School of</td>
</tr>
<tr>
<td>Amy Ridenour</td>
<td>Chairman, National Center for Public Policy Research</td>
</tr>
<tr>
<td>The Honorable Ken Cuccinelli</td>
<td>President, Senate Conservatives Fund</td>
</tr>
</tbody>
</table>
Dee Hodges
President
Maryland Taxpayers Association