

# **Bond Case Briefs**

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## **Republicans Skeptical of Puerto Rico Chapter 9 Bill.**

WASHINGTON — Legislation that would amend the U.S. Bankruptcy Code to allow government-owned corporations in Puerto Rico to reorganize through Chapter 9 may face an uphill battle in Congress after drawing a lukewarm reception from Republicans on a House panel Thursday, despite strong support from Democrats.

Witnesses testifying before the House Judiciary Committee's subcommittee on regulatory reform, commercial and antitrust law, which has jurisdiction over bankruptcy law, mostly expressed strong support for the bill.

The Puerto Rico Chapter 9 Uniformity Act of 2015 is sponsored by Democrat Pedro Pierluisi and has bipartisan support on the island, but some major funds invested in Puerto Rico bonds oppose it. If enacted, the bill would allow issuers such as the cash-strapped Puerto Rico Electric Power Authority to formally reorganize under court supervision, something it cannot do under current law. Pierluisi introduced the bill last year but it went nowhere.

Rep. Tom Marino, R-Pa., said the potential ramifications of the legislation needed to be carefully considered because the relatively small island is a huge municipal issuer and the fate of its bonds could affect a diverse array of investors from hedge funds to small retail investors.

"Much is at stake for both Puerto Rico and investors in its debt," Marino said. "We need to be mindful of its potential broad and wide-ranging impact," he said.

Rep. Darrell Issa, R-Calif., said lawmakers would have to be mindful of whether it is their role to "retroactively" apply this change to billions of dollars of bonds that were issued and purchased under a different set of legal circumstances. He also questioned whether it is the role of Congress to grant this option to Puerto Rico when a federal court had already disallowed a local law that tried to do the same thing.

On Feb. 9 a federal court in Puerto Rico struck down the Puerto Rico Debt Enforcement and Recovery Act, a law that was enacted last year to give the island's public corporations a process to restructure their debts.

"While I've not made a decision about the bill in its current form, I have serious questions," said Issa.

The full Judiciary Committee chairman, Bob Goodlatte, R-Va., did not attend but submitted a statement expressing some of Issa's same skepticism.

"Chapter 9 of the Bankruptcy Code could provide predictability, transparency, and stability to a Puerto Rican municipal bankruptcy," Goodlatte said in his statement. "It also could serve as a framework within which parties could come to the negotiating table and reach a consensual restructuring. That said, bondholders purchased Puerto Rican bonds at a time when chapter 9 was not an option. Proposals to retroactively impact investors' rights should be reviewed with care and

caution.”

Democrats, outnumbered on the panel and unable to advance the legislation without Republican support, expressed strong backing for the law. Ranking subcommittee Democrat Hank Johnson, D-Ga., said he supports the bill because it will provide “a vital roadmap” for distressed Puerto Rico issuers. John Conyers, D-Mich., the full committee’s top Democrat, called the current exclusion of Puerto Rico from Chapter 9 access “inexplicable.”

“This is so important,” said Conyers, who represents Detroit.

John Pottow, an attorney and professor at the University of Michigan, told the subcommittee that the bill is a “long overdue” technical correction that is narrowly-tailored to grant Puerto Rico the authority already given the states to determine under whether and what conditions its political subdivisions can declare bankruptcy. Pottow said that the federal court’s decision to strike down the local Recovery Act served as “an invitation” to seek this exact remedy.

Robert Donahue, a managing director at Municipal Market Analytics, told the panel that the bill poses no systemic risk and reduces the likelihood Puerto Rico will ask for outside help to meet basic needs for its citizens.

“This is the best option among a limited set of unattractive options,” Donahue said.

Thomas Mayer, a lawyer who represents funds managed by Franklin Municipal Bond Group and OppenheimerFunds, Inc. said the bill should be killed in favor of a receivership. Chapter 9 hurts bondholders because it is slow and unpredictable he said, and PREPA should handle the situation itself.

“PREPA itself does not need Chapter 9,” he said. “It can fix itself. It can raise revenues in the same manner as nearly every other municipally owned utility in the United States. PREPA has not raised its ‘base rate’ – the rate that pays for everything other than fuel and purchased power – in nearly 26 years.”

The Puerto Rican government has warned that without reorganization authority, bondholders could take actions that would impact PREPA’s functionality such as suing to raise electric rates or asking a court to appoint a receiver who would take control of its operations. Pierluisi told Mayer he does not understand how that path could be an improvement over Chapter 9. Other debtors could also sue PREPA, Pierluisi said, providing bondholders with no certainty. But Mayer responded that events in Detroit’s Chapter 9 proceeding, where pensioners got paid more than bondholders, makes his clients concerned.

The hearing was sparsely attended by lawmakers, with only three of the subcommittee’s 13 members appearing. MMA partner Matt Fabian said that a poorly-attended hearing could indicate a dim outlook for the legislation.

THE BOND BUYER

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