Bond Case Briefs

Municipal Finance Law Since 1971

Puerto Rico Governor Spurns Federal Oversight Board's Deepest Austerity Suggestions.

Puerto Rico's governor unveiled a fiscal plan that calls for paying the U.S. territory's creditors roughly a third of what they are owed for the next decade while rejecting austerity measures prescribed by its federal oversight board.

Gov. Ricardo Rossello's fiscal plan, released Tuesday, outlines a combination of spending cuts and revenue enhancements that he says will fix Puerto Rico's 10-year, $55 billion funding shortfall while reducing the size of its government and spurring private investment.

The governor will also ask Congress to extend a legal stay that has blocked creditors from suing over bond defaults, according to the plan. A spokesman for investment funds holding general obligation bonds said the request "undercuts its professed commitment to a consensual process and, if granted, would allow [the administration] to delay negotiating with creditors."

The stay expires May 1, and hopes among creditors are dimming that Puerto Rico can lock in consensual debt deals before then.

Mr. Rossello's plan says that much of the burden of balancing the government ledger should fall on creditors holding roughly $70 billion in municipal bonds. It projects that Puerto Rico can pay $10.5 billion in principal and interest on its bonds between the 2018 and 2026 fiscal years, approximately a third of the $30 billion owed under existing debt contracts.

Market reaction to the document was muted as the benchmark general obligation bond changed hands at 74 cents on the dollar Tuesday, in line with recent prices, according to Electronic Municipal Market Access. Sales-tax bonds were also virtually unchanged.

The governor's blueprint breaks with certain recommendations of Puerto Rico's oversight board, which in January recommended sharper reductions in government payroll, pension benefits and health-care spending, as well as deeper reductions in debt payments.

The oversight board, which is supervising the territory's debt restructuring process, has veto power over the fiscal plan under the federal rescue law passed for Puerto Rico last year. The board is currently reviewing the plan, a spokesman said Wednesday.

How much money is available for creditors is highly dependent on whether Congress extends health-care funding mandates for Puerto Rico under the Affordable Care Act that are currently scheduled to lapse in December. The future of the law itself is in doubt as Republican leaders in Washington are drawing up plans for repealing the ACA and confronting internal divisions over how to replace it.

Mr. Rossello's representative on the board, Elias Sanchez, on Wednesday told The Wall Street Journal he was confident GOP lawmakers would allocate more federal health-care dollars to Puerto Rico, freeing up additional funds for creditors beyond the plan's baseline projections. The fiscal plan said that full ACA funding would more than double the moneys available for debt repayment.

The board can approve Mr. Rossello's plan or adopt its own, but an approved plan must be in place before it can initiate a bankruptcy-like process in which creditors could be forced to accept unfavorable restructuring terms. The Puerto Rico Oversight, Management, and Economic Stability Act, or Promesa, provides for a period of voluntary debt negotiations. That window is currently set to end on May 1, although Mr. Sanchez said the governor would ask Congress to extend that deadline.

The fiscal plan calls for Puerto Rico to cut its annual health care spending by roughly $300 million starting with 2019 fiscal year. The proposed health-care cuts would still leave the territory spending $700 million more a year than the board previously recommended.

The plan, which the governor discussed Tuesday in a gubernatorial address and released publicly via Twitter, cuts roughly $60 million in annual pension costs, less than the $200 million in annual retirement savings sought by the board.

Those austerity measures are based on misguided comparisons to other sovereign borrowers like Panama, Jamaica and Spain that cut government spending in the midst of financial crises, Mr. Sanchez said. Puerto Ricans are already leaving for the U.S. mainland at record rates, and an austerity regime would accelerate the out-migration, he said.

The fiscal plan addresses roughly $50 billion in debt owed by the territory but doesn't encompass its government water and power utilities, which owe a combined $13.5 billion and will develop their own plans. Mr. Rossello in January wrested control of negotiations over the only debt restructuring accord Puerto Rico has reached thus far, a $9 billion deal struck in 2015 covering the electric utility known as Prepa.

His plan also gave no indication about how the available dollars should be divvied up among competing creditor groups, though creditors holding sales-tax bonds are clashing with general obligation holders in court over who should be repaid more. Last month a federal judge refused to freeze the litigation while negotiations play out, and so far the governor hasn't taken sides with either investor group.

"We'll eventually most likely take a position," Mr. Sanchez said.

THE WALL STREET JOURNAL

By ANDREW SCURRIA

Updated March 1, 2017 5:36 p.m. ET

—Matt Wirz contributed to this article.

Write to Andrew Scurria at Andrew.Scurria@wsj.com