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How the Triple Tax Exemption on Puerto Rico's Bonds Financed Its Territorial Status - and Helped Spark Its Debt Crisis.

How did Puerto Rico manage to incur a monumental debt of $72 billion without raising red flags among the sophisticated investors who continuously bought its bonds? Here associate professor of business Evaluz Cotto–Quijano points to the role of a tax exemption designed by the US Congress over 100 years ago to finance Puerto Rico's territorial government by inflating its bond debt instead of appropriating federal funds.

On June 30, 2016, a day before the government of Puerto Rico missed a bond payment, the US Congress and President Obama passed the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA). This statute places the Financial Oversight and Management Board for Puerto Rico in charge of handling Puerto Rico's debt crisis "[to] provide a method to achieve fiscal responsibility and access to capital markets."

PROMESA excludes the government of Puerto Rico from the control of the process to restructure the crippling $72 billion debt that could threaten the stability of the US financial institutions (mainly investment companies—hedge funds, closed-end funds, open-end funds—and monoline insurance companies) that bought Puerto Rican bonds.1) Its enactment and implementation raise many questions. One, especially, comes to mind: How was such a monumental debt incurred?

In this essay, I discuss issues not addressed in most media coverage of PROMESA and the Puerto Rico debt crisis. This debt crisis, I argue, goes beyond the simplistic narrative of a profligate people redeemed by the intervention of the US government through PROMESA. I propose that the enormity of the Puerto Rican bond debt is the intended result of a US government policy dating back more than a century to finance the operations of its territorial government.2)

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