Bond Case Briefs

Municipal Finance Law Since 1971

Puerto Rico Wins Approval of $18 Billion Bond Restructuring.

Puerto Rico won court approval Monday for a restructuring deal that wipes out one-third of its $18 billion in sales-tax bond debt, a milestone in its quest to fix its broken finances.

U.S. District Judge Laura Taylor Swain confirmed a debt adjustment plan covering the revenue bonds known as Cofinas, marking the largest renegotiation yet of the U.S. territory's bond and pension obligations.

The write-downs imposed on the Cofina bonds, first issued as rescue financing in 2007, will save the island government $17 billion in interest and principal payments over the coming decades as it tries to reverse a decade of economic decline and out-migration.

Creditors holding more than $14.5 billion in Cofina debt supported the accord, which resolves one of the thorniest conflicts in Puerto Rico's unprecedented, court-supervised bankruptcy.

The settlement is tied to a negotiated split of the sales taxes pledged to Cofina that releases 46% of the money back to the island's government — providing $456 million a year on average that otherwise was earmarked for bondholders.

Judge Swain acknowledged that the settlement "commits substantial portions of Puerto Rico's scarce revenues to bond payments over a period of decades," while also slashing claims from bondholders, including individual investors who bought Cofina securities for their retirement.

But she concluded the adjustment plan "is essential to ensure that Puerto Rico is on a path that will restore its access to financial markets as it builds a stronger economy."

The settlement marks the first adjustment plan approved under the quasi-bankruptcy process created by Congress under a 2016 rescue law that also installed an oversight board to manage Puerto Rico's spending and pilot the debt- restructuring process.

The oversight board was able to wring savings from Cofina's bondholders in part because of lingering doubts about the strength of their claims on sales-tax revenue. Critics of the Cofina structure have long insisted that sales taxes never should have been transferred out of the government's control, and other creditors holding Puerto Rico general obligations said they, not Cofina bondholders, had an ironclad claim on the revenue.

First issued in 2007, the Cofina bonds were backed by sales taxes that provided investors a secure source of repayment and lowered Puerto Rico's financing costs after the municipal bond market lost confidence in the U.S. territory as a borrower.

The Cofina bonds quickly became a go-to financing source that made up roughly 40% of Puerto Rico's core government obligations when it entered bankruptcy protection in 2017.

Doubts about who owned the sales taxes — the government or Cofina's bondholders — have clouded Puerto Rico's bankruptcy since it entered court protection in 2017. Forcing Judge Swain to decide the issue could have wiped out Cofina's bondholders completely — or guaranteed them a 100% recovery if the pledge was upheld.

The Cofina plan instead relinquishes more than 46% of the pledged sales taxes, supplying cash to correct the government's budget imbalance and ameliorate politically unpopular austerity measures.

BY DOW JONES & COMPANY, INC. | MUNICIPAL | 02/04/19 05:47 PM EST

By By Andrew Scurria

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