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Puerto Rico Government Development Bank at Risk of Receivership.

Puerto Rico's Government Development Bank, which oversees the island's finances, said it may fail to comply with legal reserve requirements by the end of December, putting the bank at risk of falling into receivership.

Puerto Rico's Commissioner of Financial Institutions is examining the financial condition of the GDB, according to the commonwealth's most recent financial disclosure, posted on the bank's website late Friday.

The GDB serves as a source of liquidity for the Caribbean island and its municipalities. The bank estimates it may fall short of its legal reserve requirement by the end of 2015, according to the filing. That would put the bank in danger of operating under a receiver and further limit the commonwealth's access to funds.

"If GDB is not in sound financial condition or becomes insolvent, the Secretary of Treasury may file a petition to a Puerto Rico court for the appointment of a receiver to suspend GDB's operations and settle its obligations," according to the filing.

The bank's net liquidity as of Sept. 30 was \$875 million, down from \$1.1 billion in March. The GDB faces a \$354 million debt-service payment on Dec. 1 and is working to raise funds to meet that obligation, according to the filing.

Outstanding Debt

Puerto Rico and its agencies had \$70 billion of debt, including \$12.7 billion of general-obligation bonds, as of Sept. 30, according to the filing. Commonwealth officials are seeking to reduce that debt load by asking bondholders to take losses or wait longer for repayment through a voluntary debt exchange. The island's economy has contracted every year since 2006. It has \$357 million of general-obligation interest due Jan. 1, yet the commonwealth's cash flows show a negative balance in November, according to the filing.

Some investors believe general-obligation bonds would receive the strongest repayment because the commonwealth's constitution stipulates that those securities must be repaid before other expenses. Yet bondholders cannot require Puerto Rico to raise taxes and no physical assets of the commonwealth may be foreclosed on to raise cash to pay general obligations, according to the filing.

Available Resources

If Puerto Rico failed to make a general-obligation payment, "the bondholders are only entitled to require the Secretary of the Treasury to apply available resources according to the constitutional priority provisions and do not have the right to compel the exercise of any taxing power of the commonwealth," according to the filing.

Puerto Rico may take revenue currently used to repay certain highway bonds and convention center debt and redirect it to pay down general-obligation securities, if there are no other available resources, according to the filing.

“It is not certain what steps a commonwealth bondholder would be required to take or what proof such bondholder would be required to produce to compel the diversion of such funds from any such instrumentality to the payment of public debt,” according to the filing.

Bloomberg

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