

Bond Case Briefs

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Puerto Rico Pleads for Congressional Help as Lawsuits Are Filed.

Puerto Rico's governor on Friday renewed his plea for Congress to provide bankruptcy protection for the debt-ridden island, after two bond insurers filed lawsuits over his decision to default on millions of dollars in bond payments last week.

"Swift action from our congressional leaders is necessary and what the people of Puerto Rico deserve," said Gov. Alejandro García Padilla in a statement.

Two insurers of Puerto Rican bonds that are now in default sued the governor and other senior officials on Thursday, saying they had illegally diverted money from some creditors so they could pay other creditors in full.

The Assured Guaranty Corporation and the Ambac Assurance Corporation said in their complaint that Puerto Rico had diverted at least \$163 million that had been pledged to pay debts they had insured. Those debts were in the form of municipal bonds issued by three governmental authorities on the island.

Mr. García Padilla said the lawsuit was a sign that a dreaded "race to the courthouse" had begun, leading to "litigation pandemonium" as different creditors sought to enforce their claims on the island's resources. He called on Congress to enact legislation that would give Puerto Rico the ability to take shelter in bankruptcy, where such creditor litigation would be automatically stayed.

Democratic members of Congress have favored a bankruptcy law for Puerto Rico, but the Republicans who hold the majority in both houses have generally said they need more financial information first.

"With no legal framework to handle this impending litigation crisis, both the Commonwealth and its creditors will soon face the opposite of due process and rule of law," Mr. García Padilla warned.

Last week, Mr. García Padilla confirmed that he had used at least \$163 million — slightly less than the earlier reported \$174 million — to help make a large payment due Jan. 1 to investors who hold Puerto Rico's general obligation bonds. That type of bond is given the highest payment priority by the Puerto Rican constitution. Mr. García Padilla diverted the money by issuing an executive order on Nov. 30, starting what is called a "clawback" of funds from lower-priority bondholders.

Assured Guaranty and Ambac said in their complaint that the clawback was unconstitutional, because it "substantially and unjustifiably" impaired their contract rights under the United States Constitution. They also said they had constitutionally protected property interests in the money, because they held liens on the pledged funds.

They acknowledged that their liens were subject to being paid after the general obligation bonds, but said the use of the clawback was still unlawful under the circumstances, "namely, where other available resources exist from which the public debt could be paid."

For months, Puerto Rico has been operating on a triage basis, diverting cash away from certain programs and services and using it to pay the bills deemed most urgent. The government came under criticism in December, for example, for using \$120 million of public money to pay Christmas bonuses to public workers and retirees. The governor said he was required by law to pay the bonuses.

The two insurers asked the court to declare the clawback unconstitutional and bar the Puerto Rican government from diverting any more pledged money. Their suit was filed in United States District Court in San Juan.

The three public authorities whose bonds have been affected by the clawback are the Highways and Transportation Authority, the Convention Center District Authority and the Infrastructure Financing Authority. Although the holders of those bonds received some of the principal and interest payments due Jan. 1, those payments were made from prepaid reserves, which is considered a technical default.

The Infrastructure Financing Authority did not have the prepaid reserves in place to make the payment, and Ambac stepped in and provided \$10.3 million.

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