
Franklin, Oppenheimer Say Cofina Changes Would Harm Puerto Rico.

Mutual-fund companies holding about $10 billion of Puerto Rico securities warned that a counter proposal to the island's restructuring offer made by another bondholder group would weaken the commonwealth's ability to resolve its financial crisis.

Puerto Rico must maintain its sales-tax structure as the Caribbean island seeks to improve its finances, OppenheimerFunds Inc., Franklin Advisers Inc. and First Puerto Rico Family of Funds, wrote in a Feb. 24 letter to Representative Rafael "Tatito" Hernandez, who chairs the House Treasury Committee, and commonwealth legislators. The island has $17.3 billion of sales-tax bonds, known as Cofinas because of their Spanish acronym.

The letter follows a debt-restructuring proposal released Feb. 10 by a different investor group that includes Goldentree Asset Management, Whitebox Advisors and Metropolitan Life Insurance, which hold about $1.6 billion of senior sales-tax bonds. In that plan, subordinate Cofinas, which already get repaid every year after the senior bonds, would wait even longer to get paid down. Franklin and Oppenheimer bought various Puerto Rico securities at par, including subordinate sales-tax debt.

"Some speculative purchasers of Puerto Rico's debt, those who have purchased securities in recent months at substantial discounts, will try to offer band-aid solutions to Puerto Rico to help themselves make a quick profit at the expense of other creditors and, ultimately, at the expense of Puerto Rico itself," the fund companies said in the letter.

Restructuring Offer

The correspondence shows the tension between long-time investors of commonwealth debt whose exposure to the island is spread out among its different borrowers and distressed-debt buyers who started purchasing Puerto Rico securities about 2 1/2 years ago when prices on the debt fell to distressed levels.

Puerto Rico and its agencies accumulated $70 billion of debt after borrowing for years to fill budget shortfalls. Governor Alejandro Garcia Padilla is looking to cut the island's tax-supported debt by 46 percent through a voluntary exchange where investors accept losses on their holdings. The senior Cofina proposal was the first counteroffer to the commonwealth's debt-restructuring plan.

Commonwealth officials have warned the island may stop paying principal and interest if it can't reach an agreement with its creditors. The island faces a $2 billion debt-service payment July 1.

Revenue Projection

Puerto Rico expects to collect about $2 billion of sales-tax receipts from its 11 percent rate in the year ending June 30, 2016, including $696.3 million of dedicated revenue that the island's already used to repay this year's principal and interest on senior and subordinate bonds, according to the Government Development Bank. Whether Puerto Rico will keep that structure or change it to help repay other bonds or obligations will be a key issue for the commonwealth and its creditors as they negotiate.

Any attempt by the administration to "weaken" the Cofina structure would impair the commonwealth's ability to obtain investment-grade ratings on future securitized bond deals that would help improve the island's finances, the fund companies wrote. The Puerto Rico Electric Power Authority plans to reduce its $9 billion debt load through a debt swap where investors take a 15 percent loss and in return get new bonds that are repaid with dedicated revenue. Hernandez, the House lawmaker, filed legislation last month that would create a similar debt restructuring for the Puerto Rico Aqueduct and Sewer Authority.

The letter was signed by Daniel Loughran, who leads Oppenheimer Rochester's municipal team, and Sheila Amoroso, co-director of Franklin Templeton's municipal-bond department, and Frank Serra, president of First Puerto Rico Family of Funds, investment firms that offer shares in mutual funds to commonwealth residents and businesses.

Bloomberg Business

by Michelle Kaske

February 25, 2016 — 5:00 AM PST