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Puerto Rico Fight Is About Setting Precedents, Bond Insurer Says.

As the debate over repaying Puerto Rico's $70 billion of debt reaches a fever pitch, bond insurer National Public Finance Guarantee Corp. says it's keeping in mind broader implications for the municipal market.

The unit of MBIA Inc. is on the hook for about $8.9 billion in Puerto Rico debt-service payments, with exposure to the commonwealth's general obligations, sales-tax debt, highways securities and others. The bonds backed by the government's full faith and credit, which would recover 80 percent under the island's latest proposal, may prove the most contentious because they're constitutionally guaranteed and losses could set a benchmark for future distressed localities, National Chief Executive Officer Bill Fallon said.

"We need to do what's best for our shareholders — we do though want to make sure that anything that's done, to the extent it sets a precedent for the market, it's done in the right way," Fallon said in an interview at Bloomberg's New York headquarters.

"The issue on the G.O.s is a big one for the marketplace, because that is meant to be full faith and credit," Fallon said. "If all of a sudden they take a haircut, yes, they made it a lower haircut than anything else, but they haven't really said they take priority yet. This is one that's going to take a while to play out."

Sacrosanct Pledge?

Questions about the sanctity of the general-obligation pledge grew after Detroit filed its record municipal bankruptcy in 2013. Those creditors eventually settled on a 74 percent recovery. National backed some of those securities.

The difference between the two distressed situations is the magnitude of the debt. Detroit had $388 million of unlimited-tax general obligations, while Puerto Rico has issued $13 billion of the securities. Its constitution says revenue must be first used to pay public debt before other disbursements can be made.

Puerto Rico instead is seeking to impose losses on all types of bonds. In a revised debt-restructuring proposal released Monday, it offers a combined 74 percent recovery on general obligations and commonwealth-backed debt, up from 72 percent in its first plan that it unveiled Feb. 1. Sales-tax bonds, called Cofinas by their Spanish acronym, would get 57 percent, up from 49 percent.

Just days earlier, investors holding almost $5 billion of Puerto Rico general-obligation bonds released their own plan that would defer principal repayments for five years through a consensual exchange offer and allow the commonwealth to make an $805 million payment on July 1. National's rival Assured Guaranty Ltd. on Monday joined in support of the proposal.

Puerto Rico said it wouldn't leave money to pay any other creditors.

When it comes to a recovery rate, “each time it keeps going up, so they’re going in the right direction,” Fallon said. “But I’m not sure people are really that inclined to start talking about what the haircuts should be, because there’s not good information.”

Bloomberg Business

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April 12, 2016 — 9:09 AM PDT