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## Puerto Rico's Warning for States, Cities: You Might Be Next.

President Obama recently signed into law a highly anticipated — and much debated — rescue bill for debt-laden Puerto Rico. While the bill has its detractors, it marks a positive step toward the promise of recovery for the island. But the bill's impact could go far beyond the commonwealth's shores.

Puerto Rico, like states and many cities, can't legally declare bankruptcy. Saddled with $70 billion in debt, Gov. Alejandro Garcia Padilla's administration has spent the last few years unsuccessfully trying to reach an agreement with creditors. During that time, the commonwealth watched its tax base decline as residents fled stateside and Puerto Rican government entities defaulted on debt.

That's what life without bankruptcy protection is like for governments, Padilla said this week in a speech at the Brookings Institution in Washington, D.C. He went on to suggest that Puerto Rico, with its smaller economy and population size, might simply be farther along on a path other U.S. governments are also traveling. "We are only ahead of the curve — the curve that looms for many states and municipalities," he said. "We are forced to try the route that others have not tried before, to knock on the doors that others may need to approach in the not-so-distant future."

When asked to elaborate afterwards, Padilla explained that he was asked several times by Congress this year how a Puerto Rican rescue bill might also help troubled states. Padilla pointed to Illinois, for example, which has the lowest credit rating of any state and has struggled to find a long-term solution to its crippling debt, including its pension liabilities. "The fact is that if you go through the timeline [and look at] what's happening in other states … if they do not react in time they will face the same cliff we were facing two weeks ago," Padilla said.

At the start of this month, Puerto Rico defaulted on a $2 billion debt payment. But it did so under the protection of the rescue package referred to as PROMESA. Among other things, the law puts a temporary moratorium on litigation regarding Puerto Rico's debt and creates a seven-member financial oversight board with final say over the commonwealth's finance decisions. The board can also file debt restructuring petitions in federal court as a last resort if creditor negotiations fail.

Bankruptcy law allows states to decide whether their municipalities can file for bankruptcy — cities in about half of U.S. states are eligible — but states themselves are prohibited from declaring bankruptcy. Given the current laws, some worry that Puerto Rico's rescue plan will be used as a road map for a struggling state or city. It's not unprecedented — PROMESA's structure was inspired in part by rescue legislation for Washington, D.C., in the 1990s.

Speaking on a panel after Padilla's speech, Florida's bond director Ben Watkins called the legislation "troubling" because it sets a precedent of allowing the federal government to change how money is paid back. "You're loaning someone money for 30 years and you think you know what you'll get in return for that," he said, referring to bondholders. "And then courts come in or federal legislation comes in to trump that — which is in effect, what has happened. That's troubling to me because I'm a state's rights kind of guy."

Still, many believe that if Congress had not approved a rescue plan in time for Puerto Rico's default this month, it would have roiled the municipal market by creating uncertainty as to whether the island would ever find protection to restructure its debt.

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BY LIZ FARMER | JULY 14, 2016