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A Junta for Puerto Rico

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On Wednesday, August 31, the government of the United States finally provided the names of the persons appointed to the Fiscal Oversight Board (FOB) for Puerto Rico. The board is the main mechanism created under the Puerto Rico Oversight Management and Economic Stability Act (PROMESA, Public Law 114-187), with powers over the budget, taxes, public finances strategies, and corresponding laws.

The prolonged crisis in the economy of Puerto Rico includes severely critical public finances with a staggering $100+ billion in debt; $70 Billion in public debt and more than $30+ billion in public pension systems déficit. All this in an economy with a $68.5 billion Gross National Product and close to a decade of depression, with massive loss of employment, growing inequality, a second cycle of mass migration to the US, and with no growth in site for the next 5 years according to IMF projections.

In general there is acceptance, resignation, and sharp criticism for the Junta. Slowly the people are awakening up to the fact that the whole federal initiative is undemocratic and colonial to start with, and secondly, that it will not solve Puerto Rico economic woes. Section 108 of the law illustrates the absolutist nature of the powers that the FOB has according to the law:

> "*Neither the Governor nor the Legislature [of Puerto Rico] may— (1) exercise any control, supervision, oversight, or review over the Oversight Board or its activities; or (2) enact, implement, or enforce any statute, resolution, policy, or rule that would impair or defeat the purposes of this Act, as determined by the Oversight Board.*" (p. 15)

The most important task of the FOB is to restore the public finances of the Commonwealth of Puerto Rico (fiscal responsibility) and regain access to credit markets under acceptable terms, after a string of defaults on debt service payments and a two year delay in publishing the last Consolidated Annual Financial Report shut the access to those markets for the commonwealth government. The most important of the mechanisms for this purpose are the (limited) Automatic Stay Upon Enactment mechanism, safeguarding Puerto Rico from lawsuits seeking repayments (Title IV), rules for Creditors Collective Actions seeking voluntary debt restructuring (Title VI), and procedures for Adjustment of Debts (Title III, described by some experts as being similar to federal bankruptcy procedures).

PROMESA also contains the Analysis of Pensions (Title II), Title IV (Miscellaneous Provisions) mandates for a Congressional Task Force on Economic Growth, a Report on Territorial Debt, and potential exemptions from the established federal minimum wage for young new workers, as well as a forthcoming new income threshold for exempt white collar workers. Title VI of PROMESA calls for the establishment of a Public Infrastructure Revitalization entity, operating under the FOB, which determines the "critical infrastructure projects" that require urgent approval with expediting rules and processes. An affirmative majority of board members is required to approve the fiscal plans and budgets, determine whether a law is not enforced, and to identify the critical infrastructure projects.

Although it is not the first oversight board imposed so far in the U.S., the fact that it is being imposed on a territory with relative autonomy in matters of self-government, similar to a state, and with neuralgic unfinished business concerning self-determination, makes the initiative a *sui generis* one as the majority of Fiscal Boards so far have being imposed on cities.

A perusal of the seven (7) bipartisan nominees (4 Republicans and 3 Democrats, plus the governor of PR as ex-officio member with no voting right) appointed to the FOB and confirmed by president Obama would seem to portray that the U.S. government addressed the concerns of democratic representation that many had regarding the Puerto Rican people's role in the FOB. Four of the seven voting members are Puerto Ricans. However, when it comes to addressing policy options for solving the fiscal crisis and economic depression what matters is not national origin but economic ideology. The fact that the operating budget for the FOB will come exclusively from the commonwealth government, with not a single dollar coming out of American citizens, (a contradiction among those who drafted the bill given that Puerto Ricans are U.S. citizens; thus, the same goes for taxpayers) reveals a lot about the spirit of the law and the agenda of the FOB members. This point of view is also shared by the White House:

> ***"****Without PROMESA, the risk that Congress might need to use tax-payer [money] to avert a humanitarian disaster in Puerto Rico only increases in the face of a spiraling, uncontrolled and disorderly crisis****".*** Jeffrey Zients Director of the National Economic Council and Assistant to the President for Economic Policy.

There is no hope among critics of neoliberal austerity policy with the FOB composition, as it is crystal clear that the majority are Republicans nominated by an extremely conservative Congress with Democrats following suit in a crucial electoral period. On top of that, the level of structural adjustment planned for Puerto Rico is certain to cause more social havoc, as a state of permanent adjustment has been in place for the last ten years and now it is about to enter the most intense phase so far.

Among the Puerto Ricans appointed to the FOB we find the names of some of the protagonists in the formulation and execution of the structural adjustment imposed by governor Luis Fortuño of the pro-statehood New Progressive Party (2008-2012), arguably the most far reaching and deep of the adjustments so far with enduring adverse consequences for the Puerto Rican economy. ***José R. González***, former president of the Government Development Bank (GDB) under the pro-commonwealth Popular Democratic Party government of Rafael Hernández Colón's second and third tenures (1986-1989), worked with the Advisory Committee for the Economic and Fiscal Reconstruction of Puerto Rico (CAREF) set up by governor Fortuño months before taking office in January 2009. The blueprint of Fortuño's disastrous economic plan came in part from the pro-cyclical austerity policy recommendations made by CAREF even though it was advised by local economists (simple Keynesianism) not to do so until private sector job creation picked up. *Even* Standard & Poor's agreed with this diagnosis at that time:

> ***"****We believe that given the dominant role that public spending has on the island's economy, the reduction in government spending without an increase in private sector employment could deepen the current recession and widen the budget deficit in fiscal 2009 and potentially fiscal 2010.*" (S&P, December 22, 2008)

During 2009 the Fortuño administration, with ***Carlos García*** presiding the GDB, did just the opposite. With law # 7 of March of 2009 a fiscal state of emergency was declared and a massive offensive was launched against public employees with a layoff of close to 20,000 public workers and a significant reduction of fringe benefits and acquired rights for the rest. The adjustment unraveled a process whose effect went beyond the public sphere through the multiplier effect, and contributed to the undermining of employment in the private sector just when the economy was nose diving with the U. S. and world financial crisis at its peak. This attack on public employment came along with regressive tax reform, the privatization of more public assets, deregulation of business permits, expanded commercial schedule with less pay for work on Sundays, increased tuition fees for higher public education (provoking two major strikes at the University of Puerto Rico), and other policies that are part of the neoliberal mantra.

The blatant hypocrisy of Fortuño's (Austerity) Plan is revealed with the massive debt emission for deficit financing under his tenure. Gross public debt rose over 30% over this period. Together with the $7 billion of American Reinvestment and Recovery Act funds, Toxic Asset Relief Program assistance, the Federal Deposit Insurance Corporation intervention for bank consolidation, and additional health funding with the Affordable Healthcare Act beginning in 2011, these funds provided a cushion for the negative effects of the structural adjustments and the global financial crisis. Still, the massive injection of local and federal funds was not enough to revert the free fall of the economy. A meagre 0.5% growth rate for fiscal year 2012 was the only significant improvement together with a brief reversal in job loss tendency.

As for the ex-officio membership of the governor of Puerto Rico, he will not be a counterbalance force within the board members. Current governor García Padilla continued the adjustment in 2013 where Fortuño's administration left it by privatizing the most important airport in the country, reducing dramatically the pension benefits of public employees, and enacting his own fiscal emergency bill. As with Fortuño, the García Padilla government's reduction of the public sector labor force continued now through labor attrition and other austerity measures. There is uncertainty about the coming elections in Puerto Rico, but a change in governor is certain given García Padilla's decision not to seek reelection. Based on previous experiences, irrespective of whether the NPP candidate or the PPD candidate prevails, the adjustment will continue, perhaps with differences in the speed and relative voracity.

Although the purpose of the FOB is "to provide a method for a covered territory to achieve fiscal responsibility and access to the capital markets," PROMESA contains other objectives regarding economic growth, critical infrastructure projects, analysis of pensions, report on territorial debt and potential labor market changes. It will be a major challenge for the FOB to juggle seemingly contradictory objectives as its mandate fits squarely in the logic of austerity. Interestingly enough, the Treasury Department of Puerto Rico recently announced it will "measure the tributary expenses that the dozens of laws granting exemptions, credits and other tax benefits would represent for Puerto Rico". Preliminary estimates suggest that around two thirds of potential tax revenues are not collected, i.e. $9.1 billion in revenues is captured for the budget out of a potential $25 billion. If this initiative is carried through and leads to a major revision of many tax exemptions and credits, a significant step will be taken towards fiscal restoration, with potential growth and development.

Much has been said about the relation between the elimination of section 936 of the Internal Revenue Code and the Puerto Rican economic decline. However, preferential taxation still applies to Puerto Rico with the Controlled Foreign Corporations regime, the same that applies to U. S. corporations currently using, for example, Ireland as a tax haven. The use and abuse of tax breaks and other forms of subsidies has taken its toll in the country's economy since the origins of Operation Bootstrap in late 1940's. Together with labor, environmental and public utilities subsidies, the economic system guarantees profits without incentivizing risk taking with more productive investment and economic activity. A major overhaul of these incentives with a fine tuned industrial policy not only could lead to economic growth, but it also would be a major step towards development as more resources are available for crucial social investment in pension systems, health, education and infrastructure.

Taking away or modifying the myriad of corporate welfare mechanisms in the country's economy will be a major challenge as it touches the very essence of internal and external class relations in colonial Puerto Rico. During seventy years, Operation Bootstrap has fed the insatiable quest for profits of corporations at the expense of social welfare. An intermediary class coalition, allied to U.S. multinationals, including local businesses, professional services providers and public administrators developed with power enough for not only keeping untouched the incentives mentioned but increasing them amidst the crisis. It's no wonder then that the primary distribution of income has being tilting more and more towards the various forms of capital income (profits and interest principally) and less towards working people. During the 2006-2015 period, net internal income grew by 18%, payments to local owners of capital increase 57%, payments to foreign investment augmented 17% while workers compensation decreased by 4%. The crisis has intensified regressive income redistribution tendencies already in place within the Puerto Rican economy and the U.S. as well. Capital income received by local residents was equivalent to 90% of what the 900,000 working people received in 2015. Local residents went from getting profits and interest equivalent to 55% of what multinationals extracted yearly in 2006 to 74% in 2015. Given these circumstances poverty is growing and inequality, measured by the Gini coefficient which is the standard measure for inequality, puts Puerto Rico as the US jurisdiction with the highest index in 2013. Puerto Rico also ranked higher in inequality than most countries in the world for which there is data, surpassing Brazil, Colombia, Honduras and Panamá.

It is under these circumstances of extreme inequality and poverty that the FOB will potentially implement austerity measures to achieve its purported aim of "fiscal responsibility and access to the capital markets." Unfortunately, and contrary to what its ideologues want us to believe, the track record for austerity as a guide for public policy during an economic downturn is both theoretically and empirically untenable. Simply put, expansive austerity does not work, i.e. there is no possibility of growth at the same time that a structural adjustment is taking place with a greater share of the income flow being set aside for equilibrating public finances, i.e. paying foreign debt. After the adjustment a country's economy may grow but the social cost of the adjustment may grossly surpass the gains from future growth. In the limit, a far reaching and deep adjustment can compromise future conditions for growth and development especially in a very fragile economy.

Interestingly enough, last Wednesday, August 31, the secretary of the Treasury, Jack Lew, highlighted the importance of embracing fiscal stimulus measures *vis a vis* austerity in a move that echoed the opinion of some within the IMF's staff -including IMF chief Christine Lagarde -that the austerity measures imposed on Greece to restructure its economy and pay of its debt were counterproductive. Also, and after the announcement of Obama concerning the composition of the FOB, Lew called on the island to submit a fiscal plan to the board while encouraging "the Board to begin its work helping the people of Puerto Rico right away.” Still, we wonder if Lew is conscious that the ideas that he now expounds, i.e. fiscal stimulus over austerity, will probably face significant opposition within a board that not only contains members of previous governments that have proudly carried the banner of austerity, but also “experts” like ***Andrew Briggs***, who is known for his conservative views on pension and social security systems, ideas well in tune with those of the institutions for which he has collaborated, i.e. the American Enterprise Institute and the CATO Institute.

More importantly, we don’t have to wait for this hypothetical situation to arise (which is also not very probable given the administrative record of the two main parties in the island) to see some of the problems of PROMESA. In a recent ruling, federal judge Francisco Besosa denied the protection supposedly provided by PROMESA and its Automatic Stay Upon Enactment (Title IV) which would safeguard the government from lawsuits by creditors seeking repayment. Several hedge-funds who own “general obligation bonds” claimed that such protection was illegal given that it violated the constitution of the island, which guaranteed and prioritized the repayment of that particular type of debt. Their lawsuit came after the government of Puerto Rico defaulted on almost $2billion of constitutionally guaranteed debt on July 1st of this year to be able to provide general services to the population. Interestingly enough, these same “general debt obligations” are under scrutiny. The preliminary results of a debt audit lobbied by unions and commissioned by the government have indicated that it was in large part acquired in an unconstitutional manner, which would make it illegal. Which of the claims will ultimately prevail is up for grabs. The current government has still not provided the resources required for the debt audit team to do its work and plaintiffs have enormous power to litigate as they see fit.

It is no secret that Operation Bootstraps became obsolete in the late 1960’s as public investment and expenditures were intensively used to sustain economic growth. The heavily subsidized model of development based on industrialization with foreign capital had its first major fiscal crisis and recession during the first half of the 1970’s. No serious attempts to reformulate the strategy were adopted. On the contrary, after the first crisis, more subsidies were allocated for attracting investment. As international competition intensified, foreign direct investment became harder to attract prompting local authorities to intensify the use of tax and all sorts of incentives. Mediocre growth, limited revenues, expanding social needs, and more corporate incentives are the main variables behind this crisis. Nonetheless, neoliberal ideology made the size of the government the culprit of the crisis, unleashing scorch earth tactics against the public sector while it was evident that the problem was not the hypertrophy of the government but the minuscule dimensions of the private sector despite all the public catering to corporate parasites whims.

If so much of a country's future was not at stake with a major humanitarian crisis evolving, these dynamics could just be considered a travesty. A long string of governments neglected its people's basic rights and well-being, while seeking to please vested foreign and local interests, political investors and themselves. These administrations managed the budget as private accounts, allocating resources with no long term vision of development and social welfare. They granted tax exemptions and credits with no rigorous analysis of the projects in question, tolerating rampant tax evasion and corruption. Then, when the fiscal nightmare burst, they declared themselves incapable of fixing it, running into the master chamber asking for help while denying any wrongdoing, asking Congress for a moratorium and restructuring of the debt, more money for a corrupt and ill designed health system, and some development tools, while claiming that it all happened because Puerto Rico is a colony with no powers at all.

Contrary to public perception that the FOB is a colonial imposition from the US government, we are certain that it is what the ruling class coalition in Puerto Rico wanted. There are two clear paths for addresing the crisis. The progressive path with deep restructuring, a strong commitment with egalitarian principles, a long term planning horizon, restoration of the environment, community based initiatives and more self-governing capacities. The second path is what has been intermittently applied to the Puerto Rican economy since the Tobin Report of 1975. It is the selective austerity policies that have perpetuated high unemployment, poverty, income inequality, mediocre growth, increasing debt, mass migration, dependence, and a lack of vision and hope for the future, especially among the young. This second path denies basic opportunity rights for the majority of the population while at the same time it allocates more resources for debt service, and corporate welfare.

It is our point of view that this crisis is, to a great extent, a *self-inflicted* one. It arises from the class bias dominating the use of powers that relative political autonomy grants, within the colonial relation, for Puerto Rico. If the crisis was self-inflicted it can be addressed, in part, with these same powers, an approach that recognizes that solving the colonial relationship with the U.S. is a necessary but not sufficient condition for disentangling the complex web of power relations that submit the needs of the people to the needs of capital and maintains relative underdevelopment in our country.

It is clear that the progressive path towards the resolution of the crisis is tantamount to a ruling class transformation and that is why the political parties that represent these interests claimed for the FOB in Washington D.C. while denying and criticizing it in Puerto Rico. Simply put, none of the major political parties wants to bear the political cost of a draconian adjustment in the island. None of those parties wants to see present internal and external power relations disarticulated.

For us it seems evident that the technocrats with the economic ideology who contributed to the present fiscal and economic crisis in our country are not capable of fixing it. On the contrary, they will make it worse. Without major income and wealth redistribution, and no sustainable growth in site (not to talk about development), we will see growing unemployment, more rationing of public services, fire sales of public and private assets, the collapse of public pension systems, more inequality and much more migration to the US. If we are to avoid emptying Puerto Rico's population in the US with a failed state and no possibility of development, structural changes cannot continue along the lines of more austerity. Just as the austerity measures didn't work then, they will not work at present unless austerity is applied to the long and generous list of corporate welfare initiatives, tax evasion and corruption both, public and private. Will the board tackle the institutional dimensions of the crisis? We don't think so.

It will be up to the people of Puerto Rico to insert themselves in the restructuring process and effectively lead it towards progressive alternatives that question and transform the power coordinates within the country and in relation to the U.S. The resources for constructing a better organized and more egalitarian society are available. The preliminary potential tax revenue figures reveal an immense and untouched quarry awaiting. Our country is full of talented and laborious people with the strong desire for better opportunities, a desire that drives many to leave and many others to stay and struggle for a better society. A long and difficult road lies ahead for the people of Puerto Rico in the era of the Junta.

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