

DEPARTMENT OF ECONOMICS

Working Paper

The Self-Inflicted Dimensions of Puerto Rico's Crisis

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“Puerto Rico requires a labor policy directed towards converting us into an attractive jurisdiction for establishing businesses and for creating opportunities of employment in the private sector”-
Francisco Montalvo Fiol, coordinator for the *Coalition of the Private Sector*, January 4, 2017.

Introduction

The decade long socio-economic depression through which Puerto Rico is passing has caught international attention, with characterizations such as “the biggest default in U.S. municipal bonds market history” or “the Greece of the Caribbean” feeding the imagination of those that seek explanations to understand it. Local and foreign bondholders, a pro-austerity government, and a fiscal control board have all become the major protagonists in a story of social decomposition in a nation that was once thought to be a model for capitalist industrial development and social welfare.

For many within Puerto Rico, past concerns and fears associated with achieving political independence from the United States, fed in large part by decades of cold war propaganda, have become very real under the colonial status. The poverty level is three times that of the United States, the island is among the most unequal nations in the world, and the emigration waves have surpassed those of the 1950s to the point that the island is being depopulated. The unhindered mobility of the “factors of production,” i.e. capital and labor, that for decades has characterized the business environment in the island has not produced the dynamic and long term economic growth, or convergence with the metropolis, that some economic theories and models would have predicted.¹

Not surprisingly many explanations have been put forward to understand the causes of the crisis in Puerto Rico. For example, some have focused on the expiration in the year 2006 of a federal tax break for corporate income that had attracted foreign multinational firms since the mid 1970s, while others point fingers at incompetent governmental administrations. Still, it is the more general topic of the colonial relationship with the United States that has taken center stage in the discussions pertaining to the crisis.

¹ For a detailed empirical description of this divergence and economic collapse, see Argeo T. Quiñones-Pérez and Ian J. Seda-Irizarry, “Wealth Extraction, Governmental Servitude and Social Desintegration in Colonial Puerto Rico” *New Politics* 15, no. 4 (Winter 2016): 91-98. For a discussion of the “Lewis Model” of economic development that was fashionable during the 1950s and how Puerto Rico’s experience did not align to it, see Francisco Catalá, *Promesa Rota: Una Mirada Institucionalista a Partir de Tugwell* (Puerto Rico: Ediciones Callejón, 2013).

Many point to the fact that March of 2006 marks the beginning of the decade long economic downturn, and given that it took place two years prior to the global economic crisis, it is seen as evidence that the crisis followed the internal clock of Puerto Rico that is tuned *primordially* to the colonial status. On top of that, 1) the double standard concerning the lack of application of Chapter 9 of bankruptcy law to Puerto Rico while it applies to municipalities of the union, 2) the imposition of cabotage/merchant laws, 3) the recent declarations and acceptance of Congress regarding the colonial relationship, 4) the lack of monetary policy, etc. all combine to seemingly give credence to understanding the fiscal crisis and economic depression *exclusively* on the basis of the submission of the island to, and the limits imposed by, the U.S. government.²

An Alternative and Complementary Analysis

There is no question that to understand the present situation in Puerto Rico one cannot simply turn a blind eye to the colonial history and status of the island, which implies that any solution to Puerto Rico's socio-economic catastrophe is not solely economic but, more importantly, political. Still, we depart ways with many analysis that understand the situation of Puerto Rico solely from a nation-state perspective using as an entry point to their analysis the politico/juridical dimensions of the colonial situation. What worries us in these accounts is that politics is reduced to the relationship between the United States and Puerto Rico, a perspective in which the island and its population are conceived simply as victims of the metropolis without differentiating groups within the island's population. This macro view of the situation, which uses nations as the unit of analysis, has lent itself in many analysis to obscuring and even erasing the internal relations of power within the particular internal class structure of the island, relations that shape and are shaped by the nation-state level analysis. We believe that this is a mistake that has pretty much led to an absolute silence on fundamental issues that have direct political consequences in relation to potential strategies that seek solutions to the crisis.

To start remedying the problem outlined above, an important methodological and political move is to differentiate the crisis of the colonial regime of the Commonwealth of Puerto Rico from the crisis of the economic model, while recognizing that both are intertwined. This clears the path for adding more relevant protagonists to the story of social decomposition whose presence is hidden behind the eternal discussions on the colonial status. A serious approach needs to examine the role that local groups have had in the looting of the public coffers and in the extraction of wealth from the colony. We join other social theorists in recognizing that in this day and age no external attempt

² See Linda Backiel, "Puerto Rico: The Crisis is About Colonialism not Debt," *Monthly Review* 67, no. 5 (October 2015).

at exploiting a country and its population would be successful if its not “rooted in coincidences of interest between local dominant classes and international ones.”³

In the case of Puerto Rico, these classes have benefitted from the *relative autonomy* of the government and its perpetuation of the failed dependent economic model that has been in place since the 1940s. When looking at Puerto Rico as a colony of the United States one cannot forget the control that the various government administrations have had in 1) altering and applying the tax system and 2) in deciding how public funds would be used. Because of the motives and outcomes of these choices, and the space for maneuver within the colonial relationship of those that took these decisions, we claim that the crisis can be understood, in important ways, to have been *self-inflicted*. In our analysis we place this recognition within the context of the perpetuation of an exhausted strategy for growth and development that had become obsolete, if it ever was successful in its purported aims, by the 1970s when the first post-war fiscal crisis hit.

By approaching the crisis this way the ending of the colonial relationship becomes a necessary but not sufficient condition for solving the problems of the victims of the crisis. It is true that to understand the development of the local elites and intermediaries, their relation to the state and foreign capital, and their general position within the economic model, one has to examine the history of colonialism in the island.⁴ Still, the particular local determination of how public resources are obtained and used within the logic of the existing economic model is one that can be reproduced even if the colonial status of the island is changed, especially if the grid of internal power relations is not addressed. The fact that certain groups and individuals have benefitted immensely from the crisis should point to the relevance of our approach.

Between 2006 and 2016, while data about “payments to the rest of the world” showed that these outflows had increased by 19% over the decade, data on the functional distribution of income pointed to a decrease in income of 3.9% for those whose income is based on employee’s compensations while income based on property (profits, interests, etc.) increased by 59%. In the year 2006 the total income based on property amounted to 56% of the total income based on employee’s compensations. By 2016, that proportion had increased to 92%.⁵ Also, as mentioned before, inequality is soaring, with the island’s GINI index (a standard measure of income inequality) standing

³ See Fernando H. Cardoso and Enzo Faletto, *Dependency and Development in Latin America* (Berkeley: University of California Press, 1979): xvi.

⁴ For a historical description of this process, see James Dietz, *Economic History of Puerto Rico: Institutional Change and Capitalist Development*, (New Jersey: Princeton Academic Press, 1986).

⁵ Authors’ calculations based on Junta de Planificación, “Statistical Appendix,” *Economic Report to the Governor*, (Puerto Rico, 2015, 2016): table 11.

at 0.559 in 2015, higher than those of Washington DC (0.535) and New York (0.514).⁶ In global terms, the levels of inequality place Puerto Rico among the most unequal countries in the world, joining the ranks of Zambia, Honduras, South Africa and Namibia. These and other statistics show the redistributive effects of the crisis. Simply put, not everybody in the island is experiencing the economic depression in the same way, which lends credence to the hypothesis that there are groups within the island that want to keep the present arrangement relatively intact.

In what follows we show various instances of policies that have perpetuated the basic contours of the failed economic model while also highlighting the continuous neoliberal structural adjustment that has been applied during the decade of depression. While a more detailed and comprehensive study is needed to disaggregate the class structure of Puerto Rico in terms of inter and intra class conflicts, and to connect it with global forms of capital (financial, industrial, and commercial) with neoliberalism as a background, we believe that the evidence provided below solidifies the first step in this endeavor: to recognize that groups within the island, in concert with the various administrations of the main political parties, have benefited for years from the current socioeconomic arrangement within the colony and that they actively intercede to preserve it.

Perpetuation of a failed model

The double-whip of the fiscal crisis and the economic depression and its effects on a significant part of the population have highlighted the structural problems of the economic model of industrialization by invitation that were identified over four decades ago when the first post-war fiscal crisis hit the island's economy.⁷ Ever since industrialization took off with "Operation Bootstrap" in the late 1940s, and throughout its different phases of light, heavy, and high-tech industries, the state has been used as an active provider for private capital, both local and foreign. Not surprisingly, what also has been constant during this time period has been the neglect of a comprehensive, well-defined industrial policy by the different governments that seeks to satisfy the needs of the population in a sustainable way. Instead, export-led industrialization and growth based on incentivized external capital flows has been the norm.⁸ The foreign direct investment to support the industrial enclave dominated by subsidiaries of multinational firms has been attracted using various incentives with no clear objectives attached to

⁶ See U.S. Census Bureau, *American Community Survey*, (1-year estimates 2015), <https://www.census.gov>

⁷ See James Tobin et al, *Informe al Gobernador del Comité para el Estudio de las Finanzas de Puerto Rico* (1976), <https://www2.pr.gov>, and José Villamil, "El modelo puertorriqueño: Límites del crecimiento dependiente," *Revista Puertorriqueña de Investigaciones Sociales* 1 (July-December, 1976): 3-14.

⁸ Comentario sobre Plan Chardón/Tugwell como excepciones a la regla?

them. Multiple tax credits and exemptions, environmental subsidies, subsidized public utilities and land, plus an abundant, educated, and cheap labor force combined with industrial peace through anti-union policies have provided a bonanza for capital. In the meantime, double digit unemployment, poverty and emigration have all been constants of the “industrial development” process.⁹

This industrialization process has historically undermined local producers and providers, causing the creole capitalist class to focus mainly on commercial and financial activities while still integrated to the state and its various governments to guarantee their profits, reminding us of Marx’s dictum that “as long as capital is weak, it relies on crutches” (Marx, 1973: 651). During the decade long depression their private needs continue to be satisfied by governmental administrations that keep playing to the tune of more tax incentives to supposedly encourage both foreign and local investment. The evidence is overwhelming.

In the year 2004, two years before the economic crisis erupted in the island, there were approximately 40 tax exemption laws for the private sector. As the crisis started gaining momentum, more tax incentive laws were passed. By the year 2008 there were around 60 of these laws. Now, in the middle of a decade long economic depression with a profound fiscal crisis where the debt to GNP ratio is around 100% (not counting net pension liabilities), there are more than 90 tax exemption laws that negate a substantial flow of income to the government in an economy that has, on average, contracted 1.5 percent per year during the last decade. What is more astounding is that these laws have not been systematically revised and, along with other types of subsidies, their numbers keep increasing.¹⁰

The Department of the Treasury calculated that between the years 2008 and 2014 total tax credits awarded by the government amounted to \$1.5 billion dollars. Still, the success of these credits was questioned by a study commissioned by the House of Representatives, which also emphasized how there had been no follow up evaluations regarding the effectiveness of these credits after their implementation.¹¹ Changes in circumstances, which at some point might have warranted the use of these incentives, and mismatches between substantial allocations and sectoral performances were also identified. For example, more than \$170 million dollars in tax credits were awarded

⁹ For accounts of the model and its limits, see Quiñones-Pérez and Seda-Irizarry (2016) and James Dietz, *Economic History of Puerto Rico: Institutional Change and Capitalist Development*, (New Jersey, Princeton Academic Press, 1986).

¹⁰ In March of 2017 the present governmental administration announced it would freeze some of these laws in what, in the best case scenario, is a short term accounting exercise with still no comprehensive analysis of their effects.

¹¹ See Ramón Cao García, et al. *Evaluación de Beneficios y Costos de Créditos e Incentivos Contributivos a Empresas*, (Unpublished, 2014).

between 2008 and 2014 for the tourism sector, a substantial amount if one takes into account the relatively small size of this sector (6%) in relation to the economy (manufacturing accounts for around 48%). On top of that big capital and its luxury hotels have been bailed out by the government on debt they defaulted on, a loss estimated at around \$419 million dollars.¹² These and other examples led the head economist of the House of Representatives study, Ramón Cao García, to go as far as to conclude that “it would be cheaper for the state to directly make the investments that it wants to promote given that their yield would go to the government.”¹³

At the level of municipalities we also see the finances undermined by tax exemptions. An estimate by the Center for the Collection of Municipal Income (CRIM) calculated that for the fiscal year 2012-2013, municipalities stopped receiving around \$900 million based on property taxes. As of now various municipalities, especially small ones, are practically bankrupt, with no money for payroll, debts that have not been serviced, and suspended projects with no financing.

Finally, the continuity among administrations in the perpetuation of the failed model of providing tax incentives with no strict monitoring to supposedly encourage employment creation and economic growth can also be seen in their recent efforts to attract foreign investors (law # 22) and to export local services (law # 20). These tax exemption laws, passed in 2012 under the tenure of Luis Fortuño (2009-2013) of the pro-statehood New Progressive Party (NPP) and promoted by the administration of Alejandro García Padilla (2013-2017) of the pro-commonwealth Popular Democratic Party (PPD) that followed, became spearhead of the economic approach. The present administration of the NPP has followed suit and provided even more flexibility for firms under these laws, which have been the main “strategy for economic development for the last 4 years, at least coming from here at the Department for Economic Development and Commerce” according to its current secretary, Manuel Laboy.¹⁴

As can be expected from these and other examples, the silver platter provided to both local and foreign capital amounts to a substantial quantum. According to a former head of the treasury, the plethora of exemptions, deductions, credits, and all types of incentives amount to an estimated \$25 billion dollars that the state could potentially

¹² Notable here is the default on the payment of a debt of \$33 million dollars of a golf resort owned by Donald Trump. The Puerto Rican government and its taxpayers eventually paid that bill.

¹³ Quoted in Laura Pérez Sánchez, “Multimillonaria apuesta que no ha rendido frutos”, *El Nuevo Día* (February 22, 2015): 4-5. www.elnuevodia.com. For details regarding the failure of these laws in realizing their purported aims, see also Laura Quintero, “Dádivas contributivas a empresas dejan poquísimos empleos”, *Noticel*, (May 6, 2015). www.noticel.com

¹⁴ Quoted in Miladys Soto, “Impulsarán Inversión con enmiendas a leyes 20 y 22”, *Metro* (March 7, 2017) www.metro.pr.

receive. Under the present arrangement the General Fund only receives around \$9 billion dollars annually in revenues.¹⁵

In general, most tax reform projects since the mid-1980s till the present have been class biased as they involved lowering taxes to corporations in order to supposedly incentivize investment and economic growth. This failed supply-side strategy has had as a result income and wealth redistribution to the top, the perpetuation of a double digit unemployment rate that has been the norm since industrialization commenced in the 1940s, and a restraint on the growth of government tax revenue.¹⁶ Also, and in a complementary redistributive way, whenever the government wants to raise money via an increase in taxes, it does it via regressive ones (e.g. sales tax increase from 7% to 11.5% in 2015, currently the highest within the U.S.).

All of the above examples provide just a snippet as to how the coffers of the government of Puerto Rico are being used for the benefit of local and foreign capital during the decade long economic depression to enforce an economic model that did not serve the needs of the population even during its so-called “golden period” of 1947-1973 when the economy grew on average 6% per year. Add to this scenario the estimates by previous comptrollers and other agencies that show that the waste of public funds via corruption schemes amounts to around 10% of the budget, equivalent to \$900 million of the general fund and \$2.9 billion of the consolidated budget.¹⁷ Also, the tax evasion rate hovers around 30% of potential revenues and there were an estimated \$4 billion dollars in uncollected taxes in 2015. Studies have pointed out that, historically, tax evasion is more commonplace as one moves farther up the income scale in the island.¹⁸

Probably the most telling hit to the coffers of the Department of the Treasury, was based on what could be termed a “local entrepreneurial boycott” when in April of 2014 over 21,000 businesses (around 33% of the total in the island) did not submit their income tax returns, even after a time extension was granted for them to do so. What makes this more revealing is that no systematic investigation was undertaken to process these firms after they did not submit their taxes. This meant that the Department of Treasury lost an estimated \$400 million dollars in state revenues, a significant amount if we take

¹⁵ These numbers were publicly shared to the media in August of 2016 by the then secretary of the treasury, Juan Zaragoza.

¹⁶ The unemployment rate of 10.3% during 1969-70 was the lowest ever recorded since 1947.

¹⁷ See EFE Agency, “Corrupción es la principal amenaza en Puerto Rico”, (June 26, 2009).

¹⁸ See Ramón Cao García and Aixa Cruz Pol, “Control de la evasión tributaria y equidad fiscal: Un análisis de la experiencia en Puerto Rico 1987 a 1997, *Ensayos y Monografías*, no. 116, (Río Piedras, Unidad Investigaciones Económicas, Universidad de Puerto Rico, 2003) <http://economia.uprrp.edu>.

into consideration as a comparative example that the government of Puerto Rico defaulted on a debt payment of around \$400 million dollars in the summer of 2016.

The lack of accountability and controls, combined with the structurally provided corporate welfare, continues while the fiscal crises and economic depression deepen. As we have seen, the incentives provided to firms have not been monitored, while their operations to enhance profits pass under the fiscal radar. Businesses that have operated for years in manufacturing, retail, and other sectors report that their economic activities produce minimal profits, break even, or even engage in losses, hiding their revenues through “profit-stripping” strategies with transfer pricing and income shifting creative accounting to pay less taxes.¹⁹

The experience of Puerto Rico’s economy is also symptomatic of the post Bretton Woods neoliberal capitalist era of world of financial flexibility that has undermined the finances of governments and the performance of economies around the world. Since 1976, when section 936 of the internal revenue code provided firms with more flexibility to repatriate their earnings, a growing mass of reported profits estimated now to be around \$30 billion dollars per year leaves the island and is not reinvested in the local economy.²⁰ Still, as we have seen before, Puerto Rico didn’t have to wait for neoliberalism to arrive for there to be both increasing private gain and an increasing socialization of costs. These outcomes were embedded in the model of industrial development since its inception in the 1940s and the current fiscal crisis is the result of it.

The fact that the economy is so dependent on foreign capital that is heavily subsidized and not linked to the local economy (more than 80% of what is consumed within the island is imported while less than 15% of the purchases done by multinationals are from local suppliers), and that this capital can move its profits around freely with minimal investment in the island’s economy, also points to the limits of potential Keynesian type expansionary policies in the island. Simply put, the lack of links between the enclave and the local economy circumvents any possibility of a positive expansionary multiplier effect on growth. Add to this the miniscule dimensions of a stagnant local private sector subsisting on a state that operates as a tax haven and, not surprisingly, you have in place a stagnant economic model of extreme wealth extraction and unequal distribution. But the problems do not stop there. Other tools that also highlight the self-inflicted

¹⁹ For an analysis of Puerto Rico’s place in the circulation of global profits, see Argeo T. Quiñones-Pérez, “Ganancias Globales y la Economía de Puerto Rico”, *Boletín Asociación de Economistas de Puerto Rico* 1, no.3, (September-October 2006): 3-5.

²⁰ The high-tech stage of industrialization in Puerto Rico is tied to this shift. Although section 936 was eliminated in 2006, preferential taxation still applies in Puerto Rico through the regime of Controlled Foreign Corporations.

dimensions of the crisis have been locally deployed during the decade of depression to squeeze and exploit large sectors of the population.

Expansive Austerity

The various administrations that have governed Puerto Rico during the decade of depression and fiscal crisis have not only continually relied on tax exemptions and credits as forms of policy, but they have also engaged in a continuous and systematic neoliberal structural adjustment. This strategy, endorsed by the ruling extractive elites of the island, has four main ideological components:

- 1) An emphasis on the “excessive size” of the government,
- 2) An understanding that people living beyond their means,
- 3) The need for a national adjustment in which all sectors of society must sacrifice and contribute
- 4) The need to keep costs of doing business low in order to maintain competitiveness.

As with tax exemptions and credits, other types of public policy have centered on the private sector of the country and abroad to try and create a supposedly better investment environment for capital. Some of the policies applied include: the privatization of public assets, the firing of thousands of public employees, tax reform favorable to the rich, the deregulation of business permits, increases in tuition fees for higher public education, cuts in public services, and the slashing of budgets of public offices. Economic growth and the ability to repay the debt of the island to regain access to credit markets was supposed to flow out of this structural adjustment.

Unfortunately, and contrary to what its ideologues want us to believe, the track record for expansive austerity as a guide for public policy during an economic downturn is both theoretically and empirically untenable.²¹ Simply put, expansive austerity does not work; 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 debt.

Probably the most emblematic example of the expansive austerity approach in Puerto Rico happened during the tenure as governor of Luis Fortuño from the NPP (2008-2012). Against the recommendations of various local economists, Fortuño passed law #

²¹ See Nina Shapiro, “Keynes, Steindl, and the Critique of Austerity Economics” *Monthly Review* 64, no. 3. (July-August 2012).

7 in March of 2009 to slash government spending.²² With this law a fiscal state of emergency was declared and a massive offensive was launched against public employees, with a mass 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 further 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, which echoes the hypocrisy of Republicans in the U.S. who have historically claimed to be fiscal conservatives, was 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, the 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, all 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.

Alejandro García Padilla of the PPD, who succeeded Fortuño as governor, continued the adjustment in 2013 where his predecessor 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.²³ As with Fortuño, the García Padilla

²² Even *Standard & Poor's* had warned against using austerity three months earlier when a report declared: "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)

²³ See Legislative Assembly of Puerto Rico, "Government of the Commonwealth of Puerto Rico Special Fiscal and Operational Sustainability Act", (June 17, 2014). <http://www.gdb-pur.com>.

government's reduction of the public sector labor force continued now through labor attrition and other austerity measures.²⁴

Finally, the current administration of the New Progressive Party (2017-present) has been very clear about its guiding ideology when, months before ascending to power, their then candidate for governor Ricardo Rosselló expressed the view that they "must once and for all dismantle the current government apparatus that is costly and ineffective [and] we should simultaneously implement real and strong free market reforms that open up our economy and lead to robust growth and job creation".²⁵ Now in office, Rosselló's labor "reform" law (January 2017), which was supported by important groups within the island's private sector, is the latest version of the continued attack on workers by both administrations, an attack that in true neoliberal vein calls for more "flexibilization" of the labor market.

In the decade of continuous neoliberal structural adjustment, the results speak for themselves. Apart from increasing inequality and poverty we have that:

- a) Total economic contraction of the economy for the period, measured in gross national product terms (GNP), is 15.2%.²⁶
- b) Non-agricultural wage labor has fallen by 16% (168,000 jobs)²⁷
- c) The real-estate market has suffered a general collapse in terms of loss of value, mortgage foreclosures and abandoned housing properties.²⁸
- d) There is a demographic imbalance caused by increasing waves of emigration and a lowering of the natural growth rate of the population²⁹

²⁴ See Working Group for the Fiscal and Economic Recovery of Puerto Rico, "Puerto Rico's Fiscal and Economic Crisis" (March 1, 2016). <http://www.gdb-pur.com>.

²⁵ See Ricardo Rosselló, "A New Path for Puerto Rico", *Forbes* (October 22, 2015), www.forbes.com.

²⁶ Authors' calculations. See Junta de Planificación, "Statistical Appendix," *Economic Report to the Governor*, table 1 (Puerto Rico, 2015, 2016).

²⁷ *ibid.*

²⁸ The year 2016 saw an increment of 21.6% in cases of mortgage foreclosures when in comparison to 2015, the highest in a decade. See Ruth Tellado Domenech, "Las ejecuciones de hipotecas alcanzan la cifra más alta de la década," *El Nuevo Día*, March 5, 2017, www.elnuevodia.com.

²⁹ In 2016 over 89,000 persons emigrated while in the 10 years before that the average was 60,000 per year.

These results and others, caused by the policies implemented by the two main political parties whose ideologies on the status differ, and which follow the general principles of the economic model in place, are in tune with the agenda of capital's representatives in the island. The *Coalición del Sector Privado* (a private sector coalition), and one of its subgroups, *Bonistas del Patio Inc* (a local group of bondholders), are examples of those that hide behind the eternal discussions on status while trying to shape local policies for their private gain.³⁰ During the crisis they have pushed for more corporate welfare (i.e. credits and tax incentives local and federal), lower nominal wages, privatization, and other policies that continue to deteriorate the economy, especially via the increase of labor market precarity.³¹ At the same time they appeal to identity and the fact that they are *Puerto Rican* to “demonstrate” that their interests are in tune with those of the island's residents. In the case of *Bonistas del Patio Inc* this has translated into pushing for a priority in the payment of the debt owed to them over the claims of other debt-holders. These parasitic “captains of industry”, along with the main political parties, are the modern incarnations of the barons of the sugar plantation era.

Fiscal Control Board and Beyond

During the last years of the decade of economic depression, the impossibility of Puerto Rico to service its debt obligations became the focal point of the crisis. Studies commissioned by the government and the private sector in 2015, and led by former International Monetary Fund economists, coincided in the need for the government to further apply the austerity recipe so that the public debt default could be avoided.³² It was in this scenario that local and international lobbying pushed the Congress of the U.S. to effectively impose a Fiscal Oversight Board (FOB) that would take away the relative autonomy of the Commonwealth and operate, in effect, as a debt collector.³³ This board, which is paid by Puerto Rican public funds and whose costs exceed the \$3 million dollars every month, 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. Section 108 of the law illustrates the absolutist nature of the powers that the FOB has according to the law:

³⁰ See Iyari Ríos-González, “¿Quiénes son los Bonistas del Patio Inc.?” June 2016, <https://econiapoliticapr.org>

³¹ The *Coalición del Sector Privado* literally stood behind governor Ricardo Rosselló when he presented and later passed his proposal for labor reform in January of 2017.

³² Prominent among these economists was Anne Krueger, renowned all over the third world for her expertise in “helping” out countries in need via IMF intervention.

³³ For an analysis of this conjuncture in which the “political establishment distracts with the same old debates over statehood and independence”, see Argeo T. Quiñones-Pérez and Ian J. Seda-Irizarry, “Politics, Primaries, and Crisis in Puerto Rico” (teleSUR, June 2, 2016), www.telesurtv.net.

“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)

Although it is not the first oversight board imposed in the U.S., the fact that it was imposed on a territory that had 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. Also, and very important for the purposes of this article, there is continuity between the board, previous administrations, and factions of capital that contributed to the increase in the debt burden during the decade of depression.

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. One of these creole appointees, José R. González, was the 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), and worked with the Advisory Committee for the Economic and Fiscal Reconstruction of Puerto Rico (CAREF) set up by governor Fortuño a few months before taking office in January of 2009. The blueprint of Fortuño’s disastrous economic plan, which we highlighted above with law # 7 (firing of around 20,000 public employees), came in part from the pro-cyclical austerity policy recommendations made by CAREF. Also, at the time of the implementation of law # 7, another Puerto Rican member of the Junta, Carlos García, was presiding the GDB.

Both García and González are excellent examples of Marx’s observation that “the public debt becomes one of the most powerful lever of primitive accumulation” as these experts “play the role of middle-man between the government and the nation, and the tax-farmers, merchants and private manufacturers, for whom a good part of every national loan performs the service of a capital fallen from heaven”.³⁴ It turns out that both of them have not only presided the BGF, but had also been executives at Santander Bank. Currently, Santander holds sales tax revenue bonds (COFINA) issued by the BGF that are part of was termed at the time “extra-constitutional”, i.e. illegal,

³⁴ See Karl Marx, *Capital: Volume 1*, (New York, Penguin Books, 1982): 919.

debt.³⁵ This situation and its evident conflict of interest have been glossed over and deemed “not problematic” in what is the usual state of business in the island.

Still, the accumulation by dispossession goes beyond these regressive and unconstitutional sales tax backed financial instruments. During Garcia’s presidency at the BGF, Santander Asset Management obtained a contract of \$270,000 to provide technical expertise regarding the management and investment of the financial assets of the public pension system, a system that as of now is insolvent. Along with UBS it was the financial consultant in the emission of \$3 billion dollars in debt that translated into over \$35 million dollars in commissions for them for the transaction and “negative investment income since day one” for the insolvent public system.³⁶ These are but two examples of the revolving door mechanism between government and capital that applies throughout the structure of the state and which has looted the public coffers to provide hefty commissions and further subsidies sustained on the basis of public resources.³⁷

In general, PROMESA and its FOB comprise the latest stage of a continuous structural adjustment that, contrary to previous local administrations, is not shy about accepting the immediate and massive negative impact of the planned austerity policies on the economy that include substantial cuts in health services, education, and retirement benefits for the sake of balancing the budget and showing “fiscal responsibility.” Their initial estimates point to a massive contraction of the economy of 16.2% for this fiscal year with no growth in site for at least a decade which, even with a substantial restructure of the debt, puts the island in a position of debt-peonage with credit markets.

Apart from the details of the austerity policies recommended by the government and approved by the FOB to balance the budget, what is interesting is that now the situation is one where the masquerade takes the form of tensions between the FOB, the government, and the bondholders, where the government hypocritically paints itself as the defender of the Puerto Rican population against the tyranny of the FOB and bondholders appeal to the constitution and its debt related sections to push for the

³⁵ Creole capitalists like GFR Media (owner of the biggest newspapers in the island) and Empresas Fonalledas Inc. also hold substantial amounts of COFINA bonds.

³⁶ For a complete analysis of this revolving door scheme, see HedgeClippers, “Pirates of the Caribbean”, (December 2016). <http://hedgeclippers.org>.

³⁷ Probably the most blatant example of the revolving-door dynamic involves the former governor Luis Fortuño and his current employer, the law firm *Steptoe & Johnson*, which received \$22.8 million in contracts while Fortuño was governor to serve as a legal intermediary in a proposed subsidy related to the 4% tax on multinationals implemented by the Obama government.

payment of what is owed to them.³⁸ While it is true that factions within the capitalist class are colliding regarding the restructuring and payment of the debt, dozens of schools keep closing, thousands of public employees keep seeing their benefits reduced, and public services keep being slashed while thousands leave the island trying to escape the adjustment. The present government reacts by juggling with the budgets of the different public branches, in what in effect is an attempt to encourage intra-class tensions.³⁹ At the same time the inter-class dynamics keep being obscured by the “frictions” at the top (government, FOB, bondholders) and the eternal debates regarding the colonial status.⁴⁰

Conclusion

A long string of governments in Puerto Rico, supported by the local elites, neglected their 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 simply 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 general visions for addressing 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, which has been intermittently applied to the Puerto Rican economy since the Tobin Report of 1975, is the selective austerity policies that have perpetuated high unemployment, poverty, income inequality, mediocre

³⁸ An example of this show is the submission by the government of what turns to be an unreal budget to the FOB for its approval, with the latter rejecting it and the former using this rejection as a rallying cry against the board while at the end accepting many of the boards recommendations for approval.

³⁹ An example of this predates the FOB, when the “Krueger Report” commissioned by the government recommended shifting funds from the University of Puerto Rico to the Administration of Health Insurance Of Puerto Rico (ASES). Now the Rosselló administration reacted to the latest student strike by proposing the same redistribution but in the opposite direction.

⁴⁰ Amidst the crisis, yet another non-binding status related referendum was held on June 11, 2017 that cost more than \$7 million dollars.

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 the corporate welfare.

While a more comprehensive study is required to flesh out the whole extractive scaffold in place in Puerto Rico, the parasitism exhibited by both foreign and local capital and facilitated by local administrations points to the urgent need to address class relations within the capitalist colony that is Puerto Rico. To simply understand the crisis, for example, in terms of a debt problem is to confuse the symptoms with the ailment. In general, solutions to the crisis cannot be simply seen in terms of restructuring the debt, regaining access to credit markets, developing this or that sector of the economy, injecting more money, or simply changing the status of the island. They have to also take into account the DNA of the economic model in place and the groups that have benefitted from it.

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, and they have had enough power to not only to keep untouched the incentives mentioned that have served as the basis for corporate welfare, but to also increase them amidst the crisis. It's no wonder then that the primary distribution of income has been tilting more and more towards the various forms of capital income (profits and interest principally) and less towards working people. Any political solution to the problem has to identify and take into account these internal groups.

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