The background image shows a street scene in Puerto Rico. On the left is a two-story building with a light purple or lavender facade, featuring arched windows and a balcony. A green fence runs along the sidewalk in front of it. To the right is a taller, weathered building with a yellowish-tan facade and windows with black metal grates. The sky is a clear, pale blue. The overall lighting suggests a bright, sunny day.

HEDGE PAPERS No. 20

New York City's
Public Pension Vultures
in Puerto Rico

HEDGE FUNDS PREYING ON PUERTO RICO MANAGE OVER \$550 MILLION IN NYCERS FUNDS

Puerto Rico's 3.5 million residents face frightening austerity measures in an economic crisis that is unfolding rapidly.

Hedge funds have been buying up a large portion of the island's debt, sometimes for pennies on the dollar. These hedge funds are betting on big profits if Puerto Rico is not permitted to declare bankruptcy or refinance its \$72 billion debt and is forced to repay all creditors in full.

Last month, a group of 34 hedge fund managers released a report calling on Puerto Rico to take extreme austerity measures in order to pay back debt, including big cuts to schools, universities and public services, reductions in the minimum wage and labor standards and increased taxes on working people.^[1]

These are harsh and fearsome proposals for residents of an island where 41% of the population already lives in poverty, and where supermarket items are 21% more expensive than in the U.S.

The report was an astounding demand for harsh austerity and hard times for working families in Puerto Rico, all to pay for huge profits for hedge fund billionaires.

Amazingly, three of the worst vulture funds have received half a billion dollars in investments from New York City public pension funds.

Among the hedge funds calling for these draconian measures were three in which the New York City Employee Retirement System (NYCERS) has invested over \$550 million of public employee retirement funds: Brigade Capital Management, Fir Tree Partners, and D.E. Shaw Group.

Rather than using their billions to invest in the island's infrastructure or create jobs in Puerto Rico, hedge funds are simply using the same methods that they used successfully in Argentina and Greece—preying on a vulnerable economy in order to extract huge profits. And they're doing it with the retirement funds of thousands of New York City workers, many of them Puerto Rican.

This report examines how these hedge funds, along with many others, are enriching themselves at the expense of the citizens of Puerto Rico, and the public employees and taxpayers who pay into and support the NYCERS system.

NYCERS HEDGE FUNDS IN PUERTO RICO

The following three hedge funds in which NYCERS has significant investments are also taking an active role in buying Puerto Rican debt at a discount, pushing the island to increase its borrowing, and demanding devastating austerity measures:

Hedge Fund	NYCERS funds managed ^[2]
Fir Tree Partners	\$151 million
Brigade Capital Management	\$130 million
D. E. Shaw Group	\$284 million
TOTAL	\$565 million

These hedge funds are part of the Ad Hoc Group, a group of 34 investors with a combined \$5.2 billion worth of tax-free bonds^[2] who also view the vulnerable Puerto Rican economy as an opportunity to generate huge profits.

THE HEDGE FUND PLAN FOR AUSTERITY IN PUERTO RICO

In July, the group released a report entitled “For Puerto Rico, There is a Better Way,”^[3] which makes the following demands that favor the wealthy over the people of Puerto Rico:

- **TAX BREAKS FOR THE WEALTHY, TAX HIKES FOR PUERTO RICANS.** In 2014, Puerto Rico expanded existing laws to entice hedge funds and other professional firms to locate on the island by waiving taxes on earnings and taxing exports at a nominal 4% rate.^[4] On July 1, the island’s sales tax jumped from 7% to a whopping 11.5% to help pay for bonds backed by sales tax revenue.^[5] But for hedge funds, this crushing hike is not enough—they recommend raising taxes even further on everyday Puerto Ricans in order to pay bondholders.
- **ELIMINATE THE MINIMUM WAGE OR LOWER IT.** Although the minimum wage in Puerto Rico of \$7.25 is set by U.S. standards, an advisor hired by these hedge funds has suggested that Puerto Rico be exempted from the minimum wage or be able to reduce it by a third.^[6] That would leave Puerto Ricans with a minimum wage of \$2.42 per hour.^[7]
- **DRASTIC CUTS TO SERVICES.** The report also calls on Puerto Rico to close schools and lay off teachers, despite the fact that the island already closed 100 schools last year. It also recommends limiting funding for the University of Puerto Rico, slashing Medicaid spending and reducing welfare payments, which they deem too “generous.”^[8]
- **PRIVATIZATION OF ASSETS.** In addition to their other recommendations, the Ad Hoc Group wants to see Puerto Rico sell off \$4 billion worth of publicly owned buildings, as well as privatize its energy company.^[9]

The hedge fund plan for austerity in Puerto Rico is the same as their proposals in Argentina, Greece and in New York and the United States—cuts to schools and services, lower wages and higher taxes for working people and big profits, low taxes and sweet subsidies for billionaires and the super-rich.

NEW YORK CITY PUBLIC PENSION VULTURES IN PUERTO RICO

The following is a snapshot of each of these three firms and their pattern of preying on vulnerable populations:

FIR TREE PARTNERS

Fir Tree Partners, led by CEO Jeffrey Tannenbaum, is one of the most visible hedge funds in the Puerto Rico debt trade. Fir Tree is on the steering committee of the Ad Hoc Group, working with other funds to push austerity for Puerto Rico and profits for billionaires.

Fir Tree has won big on the austerity-vulture play before, causing suffering and reaping profits in Argentinian debt crisis—and they're currently active in the crises in Greece and Puerto Rico.



Jeffrey Tannenbaum

Although Tannenbaum keeps a relatively low profile, Fir Tree made a name for itself during the Argentina debt crisis, during which it bought a large amount of Argentinian bonds at a discount and then held out for maximum repayment.

Fir Tree reportedly closed this fund last year after recording 20% annualized returns on the investment—big gains for the billionaires.^[10]

Fir Tree has repeated these tactics in Greece over the last several years, buying up Greek debt and investment stakes in Greek companies in order to profit off of the country's economic crisis.

^[11]

Now they're demanding austerity for Puerto Rico—and they've gotten over \$150 million in investments from NYCERS.

BRIGADE CAPITAL MANAGEMENT

Like Fir Tree, Brigade Capital Management sits on the steering committee of the Ad Hoc Group.^[12] And they're masters of austerity-driven profits as well.

In July, Fir Tree and Brigade, along with a subset of the Ad Hoc Group, hired the law firm Davis Polk & Wardwell to support their efforts to force Puerto Rico to make the maximum repayment to creditors.^[13]



Don Morgan

Brigade's CEO, Don Morgan, was one of the masterminds behind efforts to make big profits from the Greek debt crisis—a behind-the-scenes force for suffering.

According to The Wall Street Journal, Morgan attended an “idea dinner” at a private residence in Manhattan, in which a number of hedge fund managers traded ideas on how to make money by betting against the Euro. At the dinner, Morgan expressed his belief that Greek debt would be “an early domino to fall” in a mounting economic crisis that would eventually reach the U.S.^[14] This dinner prompted an investigation by the U.S. Justice Department.^[15]

Now Morgan is armed with \$130 million in pension money from New York City public workers for his austerity scheme in Puerto Rico—including money from Puerto Rican workers.

D.E. SHAW GROUP

D. E. Shaw Group, led by CEO David Shaw, is one of many hedge funds to reportedly use Puerto Rico as a tax haven.[16]

Yep, it's true: Shaw is pushing higher taxes for working people while enjoying low taxes for hedge funds and billionaires.

In recent years, the island passed two bills establishing a flat 4% tax rate on earning and a 100% tax exemption on exports for firms with at least three employees.^[17]

Although the legislation was intended to promote investment in Puerto Rico and its people, hedge funds have been taking advantage of the tax breaks without investing in activities that benefit the island—or even while engaging in activities that hurt Puerto Rican families.



David Shaw

D.E. Shaw is not known for making large bets against foreign currencies; however, it cut its teeth during the Greek debt crisis by betting against the Euro—and walking away with significant profits.^[18] It appears to be attempting to remake this “success” by buying Puerto Rican debt.

And Shaw is running this game with a quarter-billion dollars of retirement funds from New York City public workers.

RECOMMENDATIONS

NYCERS allocates at least \$1.2 billion to hedge funds,^[19] nearly half of which is invested in three hedge funds—Fir Tree Capital, Brigade Capital Management, and D.E. Shaw Group—that are currently betting on Puerto Rico’s economy to fail.

New Yorkers have strong ties to the island of Puerto Rico. There are more Puerto Ricans in the United States than there are in the island of Puerto Rico, and the largest population of Puerto Ricans live right here in New York City. We cannot deny Puerto Ricans’ vast contributions to New York.

NYCERS should not be paying millions of dollars in management fees to these hedge funds that are actively participating in the destruction of the livelihood of Puerto Rico’s working families.

Considering this, we recommend that NYCERS divest from Fir Tree Capital, Brigade Capital Management, and D.E. Shaw immediately.

These hedge funds should not be permitted to take profits from managing the retirement savings of the public employees of New York City—many of whom are Puerto Rican—and then use the profits to send Puerto Rico’s economy into complete collapse.

Divesting fully from these funds represents not only a strong fiduciary decision for NYCERS, but also an act of support for Puerto Ricans living in New York City and Puerto Rico.

FOOTNOTES:

- [1] <http://www.theguardian.com/world/2015/jul/28/hedge-funds-puerto-rico-close-schools-fire-teachers-pay-us-back>
- [2] http://www.nytimes.com/2015/07/27/business/dealbook/puerto-rico-should-collect-unpaid-taxes-hedge-fund-economists-say.html?_r=0
- [3] <http://www.theguardian.com/world/2015/jul/28/hedge-funds-puerto-rico-close-schools-fire-teachers-pay-us-back>
- [4] <http://www.forbes.com/sites/laurengensler/2015/02/11/puerto-rico-new-age-tax-haven/>
- [5] <http://www.nbcnews.com/news/latino/puerto-rico-legislators-approve-much-debated-sales-tax-increase-n365256>
- [6] <http://recend.apextech.netdna-cdn.com/docs/editor/Informe%20Krueger.pdf>
- [7] <http://www.thenation.com/article/how-hedge-and-vulture-funds-have-exploited-puerto-ricos-debt-crisis/>
- [8] <http://www.thenation.com/article/how-hedge-and-vulture-funds-have-exploited-puerto-ricos-debt-crisis/>
- [9] <http://www.theguardian.com/world/2015/jul/28/hedge-funds-puerto-rico-close-schools-fire-teachers-pay-us-back>
- [10] <http://www.bloomberg.com/news/articles/2014-12-04/hedge-funds-crowd-into-argentina-as-fir-tree-cashes-out>
- [11] <http://www.wsj.com/articles/SB10001424052970203406404578072821982011376> <http://www.bloomberg.com/news/articles/2013-04-10/third-point-starting-greek-focused-hedge-fund-on-recovery-bet>
- [12] <http://blogs.wsj.com/moneybeat/2015/04/14/puerto-ricos-creditors-push-for-new-bulletproof-debt/>
- [13] <http://www.bloomberg.com/news/articles/2015-07-07/puerto-rico-creditors-said-to-hire-davis-polk-as-new-group-forms>
- [14] <http://www.wsj.com/articles/SB10001424052748703795004575087741848074392>
- [15] <http://www.wsj.com/articles/SB10001424052748703795004575087741848074392>
- [16] <http://www.marketwatch.com/story/puerto-rico-woos-rich-with-hefty-tax-breaks-2014-04-22>
- [17] <http://www.marketwatch.com/story/puerto-rico-woos-rich-with-hefty-tax-breaks-2014-04-22>
- [18] <http://www.wsj.com/articles/hedge-funds-win-as-euro-falls-1426456857>
- [19] As of June 30, 2014. From NYCERS 2014 CAFR, available at: <http://www.nycers.org/%28S%28kzjhx045khuzc0v05iklbjis%29%29/about/CAFR.aspx>

WHO ARE THE HEDGE CLIPPERS?

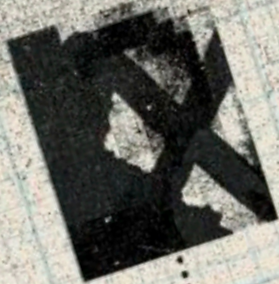
The Hedge Clippers are working to expose the mechanisms hedge funds and billionaires use to influence government and politics in order to expand their wealth, influence and power. We're exposing the collateral damage billionaire-driven politics inflicts on our communities, our climate, our economy and our democracy. We're calling out the politicians that do the dirty work billionaires demand, and we're calling on all Americans to stand up for a government and an economy that works for all of us, not just the wealthy and well-connected.

The project is supported by the Strong Economy for All Coalition, a coalition of labor unions and community groups working to fight income inequality and build shared prosperity and economic & social justice in New York and around the country.



CAPITAL ADVISORS, L.P.
CAPITAL INVESTORS, L.P.
CAPITAL MANAGEMENT, L.P.

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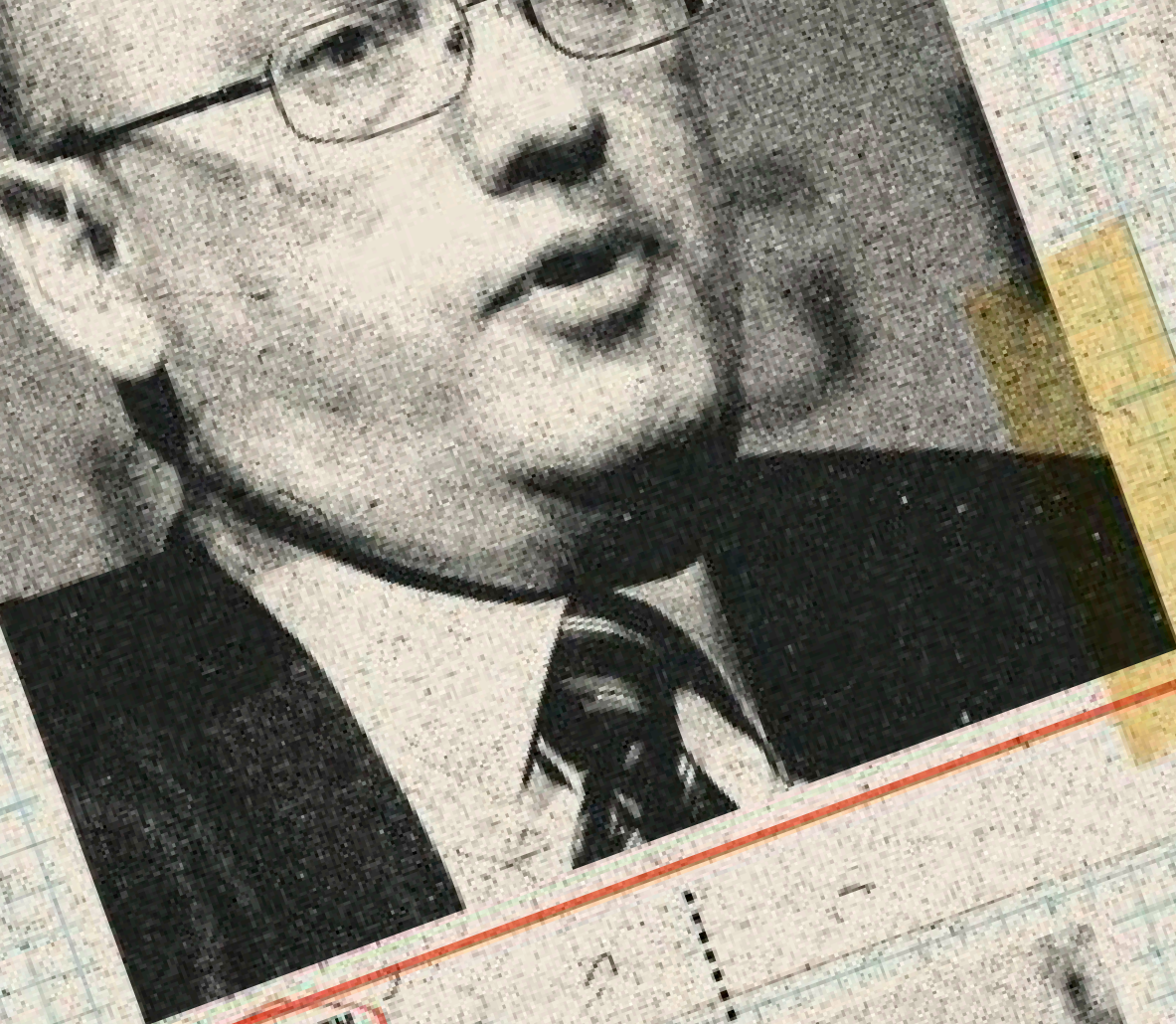


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