

# HEDGE PAPERS No.26

Puerto Rico:  
Pain and Profit

# INTRODUCTION

As 2015 came to an end, there was much speculation about the January 1st deadline for Puerto Rico to pay its creditors. There was no question that the island would default on its almost \$1 billion in debt payments, but no one knew precisely how large that default would be. When the deadline arrived, Puerto Rico defaulted on only \$37.3 million, a much smaller amount than many had feared.<sup>[1]</sup> Some bystanders speculated that because the island could still pay 97% of their debts, the government was exaggerating the extent of their crisis.<sup>[2]</sup>

That argument not only belies fiscal reality – the Puerto Rican economy has shrunk over 10% since 2006 – but also disregards the tremendous suffering the Puerto Rican government is imposing on its people in order to pay its creditors. With a poverty rate already at an alarming 45%, the island's austerity budget is quickly turning its debt crisis into a full-fledged humanitarian disaster.<sup>[3]</sup>



To pay back its creditors, Puerto Rico has resorted to extreme measures including delaying tax refunds to its citizens,<sup>[4]</sup> increasing sales tax by more than 50%,<sup>[5]</sup> and instituting massive cuts to education, healthcare, and social services. Unsurprisingly, Puerto Rico's most disenfranchised populations (including Medicaid and Medicare enrollees, incarcerated people, and families with special needs children) are shouldering the burden of those measures.

*To pay back its creditors, Puerto Rico has resorted to extreme measures including delaying tax refunds to its citizens, increasing sales tax by more than 50%, and instituting massive cuts to education, healthcare, and social services.*

The crisis is driving more Puerto Ricans off the island and onto the mainland, fueling an ongoing “population swap”<sup>[6]</sup> in which unemployed, young Puerto Ricans leave the island in search of work, while hundreds of wealthy Americans move onto to the island because the “Millionaire's Law”<sup>[7]</sup> and other policies have turned it into a “fiscal paradise” for the wealthy.<sup>[8]</sup> Indeed, 10% of the island's population has left in the last ten years and today as many as 3,000 Puerto Ricans are fleeing each week.<sup>[9]</sup> This massive depopulation has eroded the availability of services in Puerto Rico and shrunk its tax base, which the government relies on to pay for pensions, services, and its debt.<sup>[10]</sup>

Meanwhile, wealthy financiers are flocking to the island to take advantage of tax exemptions and cuts on corporate taxes, personal income, and capital gains.<sup>[11]</sup> At a recent investment conference, billionaire hedge fund manager John Paulson predicted Puerto Rico would become the “Singapore of the Caribbean”<sup>[12]</sup> –that is, an extremely wealthy tax haven.

This report details how, in order to pay back its creditors, the Puerto Rican government has implemented a severe austerity budget that is creating a humanitarian crisis on the island and threatening Puerto Ricans' access to basic services including healthcare, education, and even electricity.



Meanwhile, the hedge funds that reportedly own nearly 50% of Puerto Rico's debt continue using vulture tactics to win as big a payday as possible at the expense of Puerto Ricans.<sup>[13]</sup>



## **ROUSEMARY VEGA, CHICAGO**

Rousemary Vega is a Puerto Rican mother of four who has been living in Chicago for 33 years. She says, “When the city closed my children’s school in Humboldt Park, I realized they were taking so much

more than just a building. They were taking a major part of our community; all so school privatizers could make money and have their piece of the pie. I learned more about Wall Street banks’ predatory swaps with the Chicago school district and saw how the banks see our schools and communities as just another way to make a profit. They want our public money going straight to their profits.

And the exact same thing is happening in Puerto Rico. They want public money going to hedge funds before schools, healthcare, and infrastructure. Because of these hedge fund managers, our small mom and pop businesses in Puerto Rico are gone. Schools are closing. People are leaving the island because there are no chances for them to survive. The soul of Puerto Rico is gone. There is a saying that you can’t get blood out of a stone, but that is exactly what these hedge fund managers are trying to do with Puerto Rico.

I want to know: When will my children’s lives matter? And the lives of the Black and Brown children in Puerto Rico who look like them? Wall Street banks doing toxic swaps in Chicago and hedge fund managers refusing to let Puerto Rico access relief see us as the same. And they’re stealing from us.

If I could talk to Mark Brodsky from Aurelius Capital or Andrew Feldstein from BlueMountain Capital, I would ask them, ‘Don’t

you have enough? Haven't you gotten rich enough?' It's one thing to be a business man. It's another to be a monster.

In Chicago and Puerto Rico, people are getting educated and rising up. If we don't fight today, we won't see a tomorrow. We have no choice but to fight."



# HEALTHCARE

The combination of Puerto Rico's budget crisis and immense disparities in federal funding for healthcare on the island as compared to the 50 mainland states has spurred massive cuts to its healthcare system.



In early January, Luis Cruz Batista, Director of Puerto Rico's Oficina de Gerencia y Presupuesto ("Office of Management and Budget"), announced a series of budget cuts totaling \$254 million<sup>[14]</sup> The Department of Health was hard hit, with cuts totalling \$10 million.<sup>[15]</sup> Funding for the island's Medicare Advantage program, which serves about 560,000 people, was also cut by 11% in January.<sup>[16]</sup> Those cuts will lead to higher copays and loss of benefits.

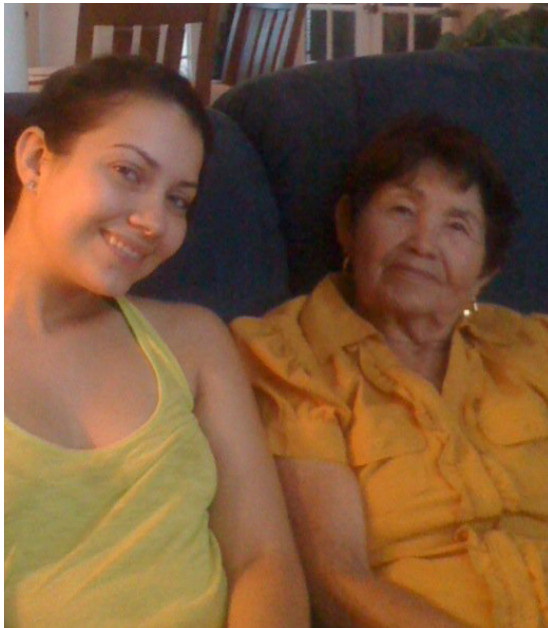
*The Department of Health was hard hit, with cuts totalling \$10 million.*

Additional cuts to Mi Salud, Puerto Rico's Medicaid program, are expected over the next two years. The effect of these cuts will be felt widely, as 45% of Puerto Rico's population – equal to 1.6 million people – rely on Mi Salud for healthcare.<sup>[17]</sup> That program

could also run out of grant money by the end of 2016 (three years earlier than expected), which could in turn lead to 900,000 people being dropped from the program.<sup>[18]</sup> Medical care experts worry that the cuts will have far reaching implications for doctors as well as patients, such as pressuring doctors and hospitals to provide services for less money, which will in turn lead to more doctors leaving Puerto Rico for better pay on the U.S. mainland.<sup>[19]</sup>

*In San Juan, “beds in hospital emergency rooms line the hallways” and the nurse shortage is so severe that people frequently hire their own private nurses during hospital stays.*

The crisis has hit hospitals and community health centers<sup>[20]</sup> especially hard. The island’s only children’s hospital cut its budget by 14% over the last two years and does not even own an MRI machine.<sup>[21]</sup> PREPA (Puerto Rico’s public power company) recently announced it would cut electricity to three clinics and hospitals that have not paid their bills.<sup>[22]</sup> In San Juan, “beds in hospital emergency rooms line the hallways”<sup>[23]</sup> and the nurse shortage is so severe that people frequently hire their own private nurses during hospital stays. The University of Puerto Rico’s Comprehensive Cancer Center’s budget was also cut by \$6.8 million.<sup>[24]</sup>



**YULISSA ARCE,  
ORLANDO, FLORIDA**

The Puerto Rican debt and economic crisis is complicated. Even with the research I have been able to do, questions of uncertainty continue to fill my head. What are the best solutions for Puerto Rico? Why is congress refusing to take up the issue? What is my family going to do?

I am the daughter of Puerto Rican’s who were born and



raised on the island. My parents were part of the wave of Boricuas leaving the island in the late 80's and early 90's, transplanting themselves and their tiny family (Me and my 2 younger brothers) in Orlando, FL in search of a better life. I grew up in Meadow Woods, the most heavily populated neighborhoods of Puerto Ricans. Growing up, it was basically just us in Florida, all of my extended family members still lived in Puerto Rico, including my grandmother, Candita Diaz Ramos.



My Grandmother is literally one of my heroes. Having worked most of her life and being the first in her family to complete some college coursework, she was definitely ahead of her time. She is strong-willed, intelligent, spiritual, and an overall amazing person. She like many Puerto Ricans started working

at clothing factories, sewing undergarments and other clothing items. But for 27 years, she worked for the public school system in Camuy, Puerto Rico as a cafeteria manager. She always expressed how much she loved her job and the joy she received each day in knowing that each student received a hearty meal. After retiring from her position at the school, she continued serving her community through her church and faith.

In recent years, life has gotten a lot more difficult for my Grandmother. She was recently diagnosed with Alzheimer's disease and has had a difficult time accepting this news. In addition, her \$400 pension, the one she worked very hard for, was gradually cut in half within the last year. Adding an increase of living expenses and on non-negotiable items such as food, medicine, and utilities, she has had to make due with a lot less. She is one of the lucky ones, because she has family in Florida that can help her, but there are thousands of elderly people living in Puerto Rico who have to choose between food, medicine, and other living expenses.

While congress ignores the plight of the 3.5 million American Citizens living in Puerto Rico and Hedge & Vulture funds continue to buy municipal debt at \$0.30 per dollar, people like my Grand-



mother have to deal with the effects of a dwindling economy and increased austerity measures being implemented by Governor Alejandro García Padilla. My family deserves better, and yours does too. We need the Federal Reserve to refinance Puerto Rico's debt and we need to get out to the polls and vote out those politicians who are in the pockets of financial interests this election. I don't need to live in Puerto Rico to help Puerto Rico. We can help now.

# EDUCATION



Last year, Puerto Rico closed 100 schools.<sup>[25]</sup> The possibility of additional cuts made headlines last summer when hedge funds holding Puerto Rican bonds released a report calling for the island to lay off teachers, close schools, and make cuts to higher education to free up money to pay its debt.<sup>[26]</sup>

Cuts have also occurred in higher education. Last spring, Governor García Padilla proposed slashing \$166 million from the University of Puerto Rico's budget.<sup>[27]</sup> Students, faculty, and staff at the university have spoken out about the ways in which ongoing budget cuts, tuition hikes, and threats to retirement benefits of faculty are decreasing the quality of education at the school and making higher education less accessible to Puerto Ricans.<sup>[28]</sup> Last summer, University of Puerto

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Rico's chair of the department of political science said that the university has "sustained a loss of \$300 million in appropriations from the general treasury"<sup>[29]</sup> over the past two years.

Students and professors are feeling the ramifications of this reduced budget. For example, when professors retire the school cannot always afford to hire replacements, leading the university to rely on adjuncts and part time professors. This also causes increases in class size. The reduced budget will also strain the university pension fund, causing it to slowly dry up.<sup>[30]</sup>

*About 2,400 students with special needs are not receiving services such as speech therapy.*

The austerity measures are also affecting special education for people with disabilities. Students have stopped attending school because the government is not paying the contractors that provide their transportation.<sup>[31]</sup> Some special education teachers have not been paid in three months.<sup>[32]</sup> About 2,400 students with special needs are not receiving services such as speech therapy.<sup>[33]</sup>

### **MILDRED ENCARNACIÓN, PUERTO RICO**

Mildred works as a maintenance person in a school for the Department of Education. During the last couple of years, she has seen how the utilities and taxes have all gone up. She worries about efforts from the government to privatize schools and save money by cutting wages and benefits from the working people of Puerto Rico. Recently Mildred was moved from her school with no notice and currently lives in fear that the next step will be massive layoffs.

### **JAMILETTE DIAZ AND PEDRO JUAN SOTO, NEW HAVEN, CT**

Jamilette Diaz, and Pedro Juan Soto came to Connecticut in March after years of fighting for better services for their son who requires special education. In Puerto Rico, Jamilette and her husband had to fight the education system to get better services. When she and



her husband found themselves with no other option, they went to legal services. There they found a free lawyer that helped them get the services that their son needed. Unfortunately, things continued to get worse in PR and Jamilette decided to move to Connecticut knowing that she would leave her family and her efforts to complete a bachelor's degree. Now in CT, Jamilette works in retail but is happy that her son is receiving the services she needs. Jamilette and Pedro, worry about what's happening in PR, they know that cuts in services will leave children like her son in a great disadvantage and that cuts in legal services will leave many without any recourse to advocate for their families.

# PUBLIC WORKERS

Puerto Rico has already implemented pension reform measures that are “more aggressive” than those that were declared unconstitutional in cases in U.S. states.<sup>[34]</sup> Successive governments enacting severe austerity measures have resulted in massive cuts for Puerto Rican public workers. Several years ago, Governor Luis Fortuño fired 30,000 public workers.<sup>[35]</sup>



**Governor Luis Fortuño, left. Right, Governor García Padilla**

In 2013 under García Padilla, the Puerto Rican government “raised the retirement age, increased employee contributions, and reduced or eliminated retiree bonuses.”<sup>[36]</sup> Recently, Governor García Padilla’s task force proposed further cuts to teacher and other public workers’ pensions as part of its package of solutions to the island’s budget crisis.<sup>[37]</sup>

*The island’s government workers pension fund was poised to go broke.*

By the end of 2015, the island’s government workers pension fund was “poised to go broke”<sup>[38]</sup> with only 0.7 percent of the assets needed to pay all the benefits promised to the 119,975 employees it

covers. This funding level is unheard of in other U.S. states--for comparison, New York State's pension fund funding ratio was 88.7 percent in 2014.<sup>[39]</sup>

And in late January, Governor García Padilla revealed that the Puerto Rican government was not putting money towards the retirement fund that covers public employees.<sup>[40]</sup> Instead, the administration had been using the fund (which is primarily funded by contributions from employees) to provide liquidity to the Treasury Department.

## **CRUZ M CONTES, PUERTO RICO**

Cruz has been working as an assistant teacher for special education in the Department of Education for 15 years. She tells us that the situation has been getting harder and harder every year and people have to choose from getting food on their tables or paying their mortgage.. Her classrooms hardly have materials and she is scared every time her payday is close that there will be no money to pay for her salary. She also tells us that taxes has gone up while salaries continue to come down. Cruz also worries about her retirement, she knows that the government is not contributing enough money and she worries that she will not be able to get the retirement that she has earned as a public servant. Cruz sees people leaving the island desperate for a better life and she is frustrated by the government's corruption, while corporations profit from our suffering.



# SOCIAL SERVICES AND GOVERNMENT VENDORS

Numerous social service programs have been slashed in the face of the debt crisis. Servicios Legales de Puerto Rico (Puerto Rico Legal Services) was forced to lay off 56 of its 288 employees in response to budget cuts. The department is facing an almost \$3 million budget deficit after its budget was reduced by \$8 million from 2010 to the present. These cuts will, of course, disproportionately impact Puerto Rico's poor, as the agency serves primarily low-income populations in cases of domestic violence, evictions, foreclosures, collection of money, custody, food, and other civil disputes.<sup>[41]</sup> The budget of the Administración de Desarrollo Socioeconómico de la Familia (which oversees programs including TANF and EBT) budget was also cut by \$3 million.<sup>[42]</sup>



The Department of Corrections and Rehabilitation budget has been cut by \$5.8 million,<sup>[43]</sup> leaving Puerto Rico's 12,500 inmates incredibly vulnerable. On January 20th, Department Secretary Einar Ramos announced that the department could no longer pay

the vendor that supplies food for inmates and was trying to reach a payment agreement with the vendor so food supply would not be interrupted.<sup>[44]</sup>

*These cuts will, of course, disproportionately impact Puerto Rico's poor.*

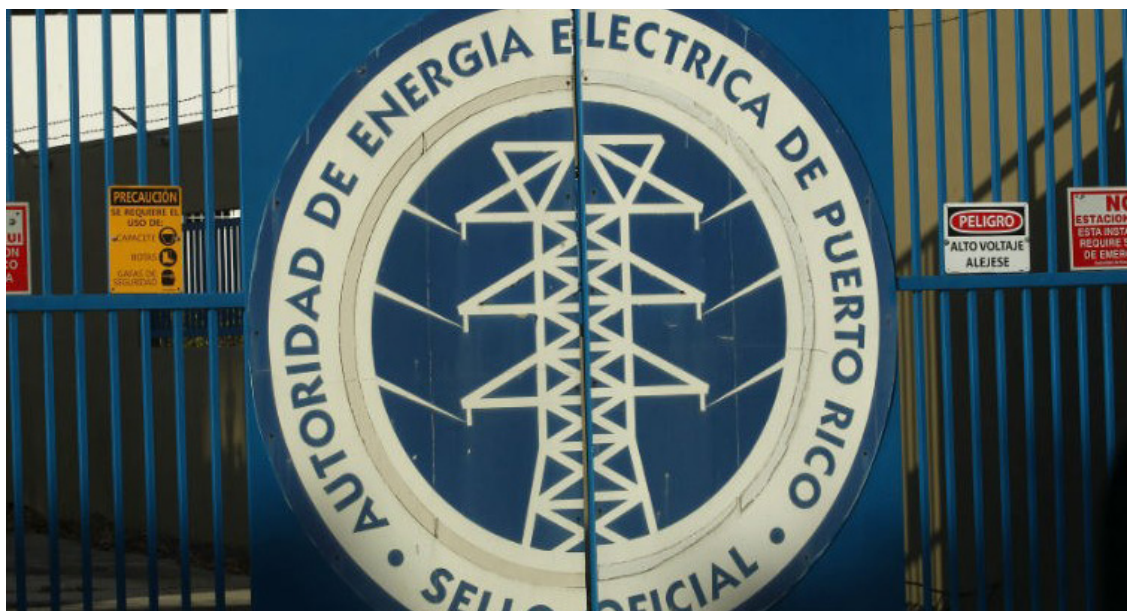


**JULIO LÓPEZ VARONA, NEW HAVEN, CT**

My father has been working at the Legal Services Corporation for more than 30 years. As a lawyer, he helps represent Puerto Ricans that come to the US to work in farms and are abused by their employers. In his work, he has helped recover hundreds

of thousands of dollars for poor migrant workers that come to the US looking work to support their families in the island. Over the years, the amount of lawyers that work on this cases has been reduced to the point that only my father does this work in the island. This year my father retires, with recent cuts to legal services my father's services and expertise will probably be faced out, leaving thousands of migrant workers with nowhere to go when faced by abuse by greedy employers.

# ENERGY



As one of the largest single issuers of Puerto Rico's debt,<sup>[45]</sup> the Puerto Rico Electric Power Authority (PREPA) has been at the center of the crisis debate. The utility has a payment of about \$400 million due to bondholders on July 1st<sup>[46]</sup> and owes an additional \$700 million to lenders that finance the shipment of fuel it burns to produce energy.<sup>[47]</sup>

Last week, a plan to restructure PREPA's debt passed Puerto Rico's House of Representatives, moving it one step closer to being signed into law by Puerto Rico's Governor. The plan, which resulted from months of intense negotiations between PREPA and PREPA bondholders, stipulates that bondholders will be issued new bonds worth 85% of face value of their old bonds with a slower payment schedule and lower interest rates. But the future of the bill is far from sealed; it has to overcome several steep regulatory hurdles.<sup>[48]</sup>

With the future of PREPA still suspect, bystanders are worried the utility could default on the largest payment yet, spurring "selective blackouts" across the island that could seriously compromise any chance of economic recovery the island has.<sup>[49]</sup> Some people close to the debt negotiations have suggested PREPA will increase rates significantly, perhaps by as much as 30 percent – the equivalent of a tax of nearly \$1 billion a year on the people of Puerto Rico.<sup>[50]</sup>



*Some close to the negotiations have suggested PREPA will increase rates by 30 percent – the equivalent of a tax of nearly \$1 billion a year on the people of Puerto Rico.*

Already, PREPA has cut services to save money. In early January, the utility announced it would cut electricity to three hospitals and clinics that have not paid their bills<sup>[51]</sup> unless a payment plan agreement could be reached. In December, the company cut off power to the Highway and Transportation Authority due to unpaid bills. PREPA also recently announced that on March 1st they will cut off electricity to public housing residents who have an outstanding balance with the utility for which they have not established a payment plan.<sup>[52]</sup>

# TRANSPORTATION

There have also been significant cuts to Puerto Rico's public transportation system. In San Juan, some buses no longer run on certain days and fares have increased to 75 cents per ride.<sup>[53]</sup> A recent \$0.30 per gallon tax increase on gasoline has also made driving more expensive.<sup>[54]</sup>



# MAKING SENSE OF THE CUTS

What do these cuts mean when they are translated to the context of the U.S. mainland?

Puerto Rico has said it may have to close 600 of the 1,460 public schools that once existed on the island in order to save money.<sup>[55]</sup> That is equivalent to New York State closing 1,861 of its 4,530 schools<sup>[56]</sup> and Florida closing 1,726 of its 4,200 schools.<sup>[57]</sup>

Up to 3,000 Puerto Ricans a week are leaving Puerto Rico every week for the mainland.<sup>[58]</sup> If this continues, 156,000 people will leave Puerto Rico in a year, the equivalent of more than twice the population of Harlem leaving New York City in a year, and more than half of Orlando, or the populations of Kissimmee, Poinciana and Buenaventura Lakes combined.



## **FATIMA GRITO, NEW YORK CITY**

Fatima Grito has been in the US for 25 years. She came from the Dominican Republic to NYC with the hopes of finding a better life and supporting her family back on the island. Like Fatima, one of Fatima's cousins went to Puerto Rico 19 years ago. In Puerto Rico, she started a family and began a restaurant business. Her business grew and they were able to expand and even have some street vendors. With the crisis, her restaurant business is in trouble, her customers have decreased and they are thinking about moving to NYC and start again. Fatima knows that she will be there to support her family if they decide to come to NYC, but she is worried about the

families that she supports in the Dominican Republic and what it will mean for her cousin to start once again from zero.

# HEDGE FUND PROFITEERING IN PUERTO RICO

## IF YOU'RE A FAMILY IN PUERTO RICO...

**If you have a child with special needs,** they cannot go to school or receive services because the government has no money to pay for teachers or student transportation.<sup>[59]</sup>

**If you live in public housing** and have an outstanding payment due to PREPA, your electricity will be turned off on March 1st.<sup>[62]</sup>

**If you are on Medicare,** your copay has gone up and you have lost benefits because the island's Medicare Advantage program's budget was cut by 11% in January.<sup>[66]</sup>

**If you are a public employee,** the government has stopped putting money towards your retirement fund.<sup>[68]</sup>

**If you are a person in Puerto Rico,** you now pay the highest sales tax in America, 11.5%.<sup>[71]</sup>

## IF YOU'RE A BILLIONAIRE IN PUERTO RICO...

**If you are David Tepper,** whose fund Appaloosa Management is part of the PREPA ad hoc group,<sup>[60]</sup> you finished construction on a \$43 million Hamptons mansion last summer,<sup>[61]</sup> soon after a hedge fund backed report suggested Puerto Rico should close schools and lay off teachers to pay back its creditors.

**If you are Ken Griffin,** whose fund Citadel is currently the sixth largest owner of Banco Popular stock,<sup>[63]</sup> you went on a \$290 million real estate spree at the end of last year,<sup>[64]</sup> buying two full floors of the Waldorf Astoria hotel in Chicago, three full floors of 220 Central Park South, a condo tower under construction in Midtown Manhattan, and a \$60 million penthouse in Miami Beach's Faena House.<sup>[65]</sup>

**If you are John Paulson,** who has been one of the most outspoken advocates of financial firms moving to Puerto Rico to take advantage of tax breaks, you have been buying up luxury real estate on the island, including La Concha Resort and the Condado Vanderbilt, two beachfront hotels in San Juan.<sup>[67]</sup>

**If you are Paul Tudor Jones,** whose fund Tudor Global Trading is a limited partner in Puerto Rico creditor Stone Lion Capital,<sup>[69]</sup> you bought a \$71 million Palm Beach estate last spring.<sup>[70]</sup>

**If you are a wealthy corporation,** for example, Walmart, you have historically enjoyed large tax subsidies on the island<sup>[72]</sup> and taken advantage of other tax dodging strategies, such as headquartering your company in Luxembourg.<sup>[73]</sup>



Some of the luxury homes of John Paulson.



# FOOTNOTES:

- [1] <http://prospect.org/article/creditors-cry-foul-puerto-ricos-default-smaller-expected>
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- [6] <http://www.jjay.cuny.edu/sites/default/files/contentgroups/economics/Seda%202%20working%20paper.pdf>
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# 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.

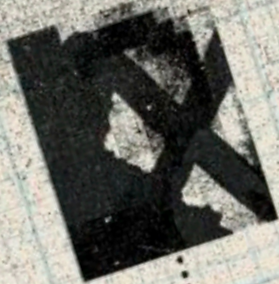
The project is supported by the Strong Economy for All Coalition, a coalition of labor unions and community groups working to fight income inequality and build shared prosperity and economic & social justice in New York and around the country.





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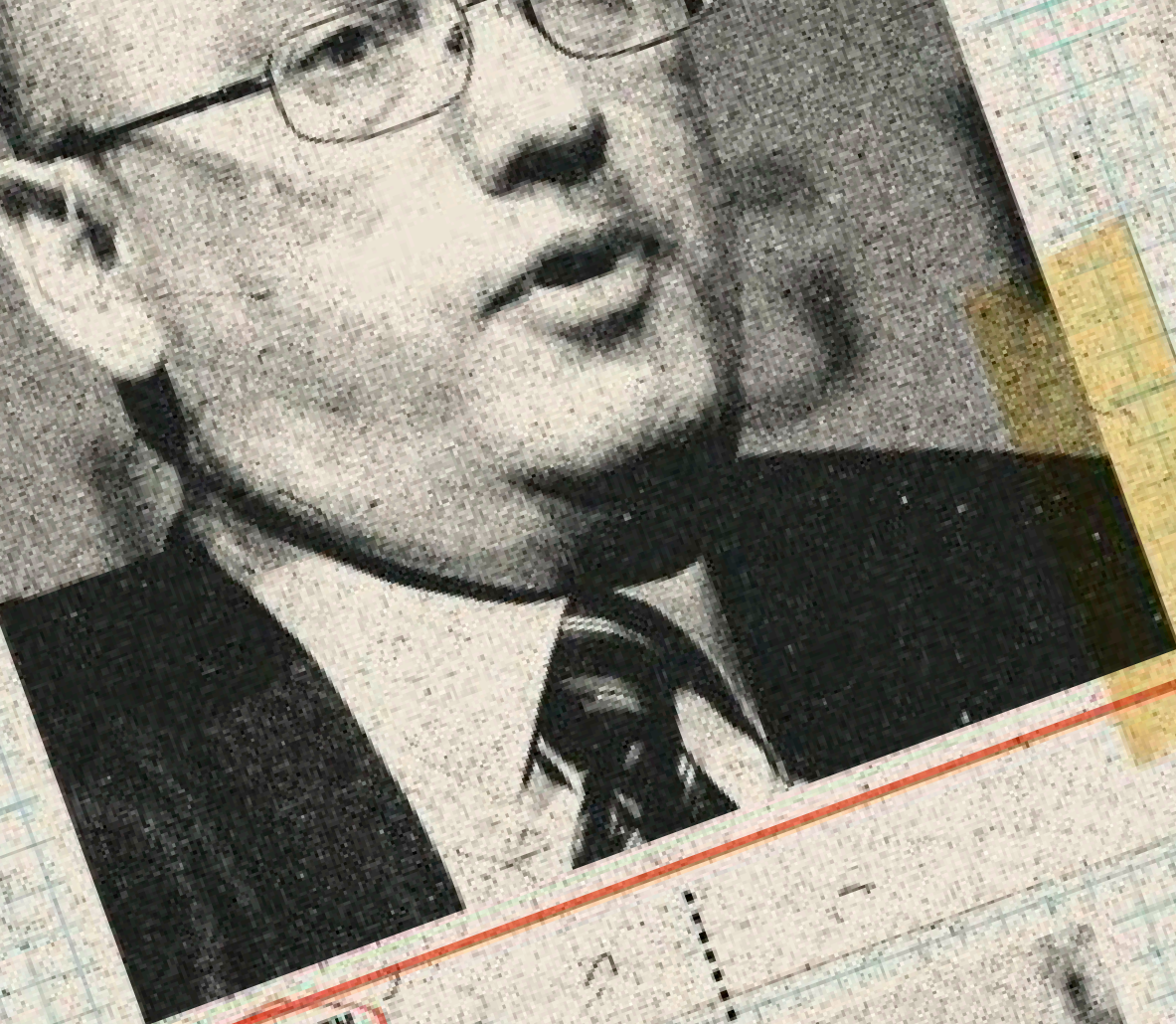
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