



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

May 2, 2016

The Honorable Paul Ryan
Speaker
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Speaker:

I am writing to follow up on my January letter regarding Puerto Rico's debt crisis and to provide information on the mounting costs of congressional inaction. More than six months ago, the Administration introduced a comprehensive legislative plan to resolve this crisis. In my January letter, I noted that absent timely congressional action Puerto Rico's fiscal, economic, and humanitarian situation would continue to deteriorate.

Since then, constructive, bipartisan discussions have taken place, and a bill has been introduced, but Congress has yet to produce a workable legislative response. Meanwhile, the crisis in Puerto Rico has deepened. In an effort to protect government deposits at Puerto Rico's Government Development Bank (GDB), the Governor has declared a state of emergency and invoked the temporary debt moratorium powers recently provided to him by the Puerto Rico legislature. Yesterday, the Governor announced that the GDB would be unable to make a \$400 million principal payment due today on its \$3.8 billion of debt. While a portion of bondholders are negotiating a restructuring of this debt, any such deal would require the participation of all GDB creditors and thus effectively would be conditioned on federal legislation providing a restructuring authority.

Today's expected default is only the latest in a series that began last summer. Since last August, the Public Finance Corporation has failed to make debt service payments on its \$1.1 billion of outstanding debt. In December, the Governor invoked his constitutional "clawback" authority to transfer funds allocated to one set of bondholders in order to pay another. This "clawback" in turn resulted in the default of \$1.9 billion of rum tax bonds and likely has put Puerto Rico on a path to defaulting on another \$5.1 billion of highway and hotel tax bonds over subsequent months.

More bond payments, some very large, are coming due soon. On July 1, Puerto Rico will face nearly \$2 billion worth of payments, including almost \$800 million of General Obligation debt. Puerto Rico does not anticipate having sufficient funds to meet these and other obligations, leaving it with the impossible choice of paying its creditors or providing essential government services. Going forward, Puerto Rico's \$70 billion of debt is unsustainable by any measure. It simply cannot afford to pay its debt. And, with a shrinking economy because of people leaving Puerto Rico, further reductions in government spending will be difficult to implement. Government expenditures, net of debt service, already have been reduced to the lowest level since 2005.

With no orderly restructuring framework to address its debts, Puerto Rico will face a series of cascading defaults. Litigation—which is already underway—will only intensify. This wave of litigation will be contentious and protracted, both among competing creditors and against Puerto Rico, and it could take many years to resolve.

This is not just a matter of financial liabilities and litigation. As I underscored in my January letter, the human costs for the 3.5 million Americans in Puerto Rico are real. And they are escalating daily. Hospitals continue to lay off workers, ration medication, reduce services, and close floors. Moreover, despite the intensifying threat from the Zika virus, financial constraints have made it extremely difficult to counteract. Unsealed septic tanks, abandoned homes, cemeteries, and piles of old tires, where mosquito larvae grow, for example, must all be treated, but the government is struggling to pay for the work to be done.

Congress must work quickly to resolve the few outstanding issues on the proposed legislation to help Puerto Rico. For example, the legislation must provide a functional and seamless debt restructuring process that initially allows for voluntary negotiations while ensuring a timely and fair resolution. The bill also must balance important policy priorities more evenly, most significantly by offering a responsible process to ensure the retirement security of the 330,000 citizens in Puerto Rico who depend on their pension benefits. Other troubling labor and federal land transfer provisions also should be addressed. Small changes in text would address these issues in a fair and acceptable way.

In the coming days, it is important to keep in mind that further inaction only gives those seeking to deter Congress from passing a bill more time to continue making inaccurate and misleading claims about the legislation. Absent enactment of a workable framework for restructuring Puerto Rico's debts, bondholders will experience a lengthy, disorderly, and chaotic unwinding, with non-payment for many a real possibility. The people of Puerto Rico will be forced to endure additional suffering. And, unless Congress passes legislation that includes appropriate restructuring and oversight tools, a taxpayer-funded bailout may become the only legislative course available to address an escalating crisis.

We appreciate you and those Members of Congress who have been working across the aisle to help put Puerto Rico on a sustainable path forward. The Administration remains committed to working collaboratively with you and your colleagues to complete action on this critical legislation as soon as possible.

Sincerely,

A handwritten signature in black ink, appearing to read "Jacob J. Lew", with a stylized, cursive script.

Jacob J. Lew

Identical letter sent to:

The Honorable Nancy Pelosi, House Democratic Leader
The Honorable Mitch McConnell, Senate Majority Leader
The Honorable Harry Reid, Senate Democratic Leader