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PARTICIPANTS:

Keynote Address:

HONORABLE ALEJANDRO GARCIA PADILLA
Governor
Commonwealth of Puerto Rico

Panel: The Muni Market in the Post-Detroit and Post-Puerto Rico Era

Moderator:

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Panelists:

NATALIE COHEN
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P R O C E E D I N G S

MR. WESSEL: I'm sure it was a great panel, I'm sorry I missed it. It's my honor to introduce to you Alejandro Garcia Padilla, the governor of Puerto Rico. The governor has been a frequent visitor in Washington for the last several months and we're really honored that he's willing to come back to visit with us today. Governor Garcia Padilla is the only governor of Puerto Rico who was actually educated in Puerto Rico, the only governor who has resided in Puerto Rico his entire life, he has a law degree from the Interamerican University of Puerto Rico. And relevant to this audience, I've learned that his wife is actually a CPA, which may or may not explain Puerto Rico's fiscal situation.

The governor is going to speak for about 15 minutes, I'm going to come back and do a brief Q & A with him, and then we'll open it up to all of you. For reporters who are in the room, after the governor is done here there's a room, a Summers room where the security guards can show you where he'll be willing to continue the conversation with reporters if you don't get a chance to answer the questions on the stage.

Thank you.

Governor Padilla. (Applause)

GOVERNOR PADILLA: Thank you, David. And about being the first governor to study and just grown up there in Puerto Rico, you will notice that in my English. (Laughter)

It is fitting to me here 10 years after the publication of Brookings' collection of policy papers on Puerto Rico, titled "Restoring Growth." That continues to be the seminal question facing the Commonwealth. Puerto Rico has been in the news for many months. Its debt and the risk of a disorderly default with the outcomes it entails, including a humanitarian crisis in the island, has attracted the attention of the United States, the Hispanic community from Spain to Argentina, and the world. The Financial Ministry of Germany hosted a visit of Secretary Lew more than a year ago and feeling the pressure put by Lew regarding Greece said that he would trade him Greece for Puerto Rico. We cannot speak for Greece, but I thank Secretary Lew for his effort for us. (Laughter)

I am sure you may have asked many times how did this situation happen. Was it overlooked, is it a surprise to Puerto Rico itself and to everybody else. You may be wondering what lesson we could all possibly learn from Puerto Rico and its leadership now that the island begins its path to financial restructuring as well as its recovery and growth. To discuss those questions I kindly accepted the invitation made by Brookings to come here today. It is a fact, Puerto Rico doesn't have the ability to repay the $70 billion debt that was generated by the island's past administration and their creators. The debt must be restructured fairly for both the people of Puerto Rico and the bond holders. A fair solution to the problem is critical in order to bring back progress to the island. States and municipalities across the United States are dealing with some of the same issues Puerto Rico is facing. The need to maintain essential service for their citizens, along with shrinking budgets and reduced federal support, the need to renovate infrastructure, to provide health services is increasing costs to all sectors of the society, to fund public pensions, to secure a competitive education for all students, rich and poor, to fight crime and drug trafficking, and to bring security to neighborhoods and streets and homes. That said, not every jurisdiction dealing with debt started with the same scenario. Certainly Puerto Rico's problems have no parallel. Puerto Rico's reality, which preceded the crisis, was unique. For instance, Puerto Rico's industrial based relied on Section 936 of the Internal Revenue Code which incentivized U.S. companies to invest in Puerto Rico rather to go to Ireland or Singapore or elsewhere in the world. It was a win-win both for Puerto Rico so people could get good jobs and the United States, which kept companies at home. Section 936 was Congress' reaction to Puerto Rico's 1970s recession due to the oil crisis, and it worked. Puerto Rico got out of recession back then.

But Section 936 was repealed by Congress in 1996 with a 10-year phase out period that ended in 2006. Companies decided to go to Ireland, to Singapore, and Puerto Rico lost thousands of industrial jobs. The effect of such an industrial construction was brushed under the rug. Industrial income -- and this is key -- industrial income was substituted by issuing debt. In December 2005, just one year before the end of the phase out of Section 936, our debt was $37 billion. Six years later, in December 2012, it was $70 billion. It nearly doubled. And in January 2013, one month later, I was sworn in. (Laughter).

The official deficit according to the Gorman back then as per documents was $333 million. The reality that came out during the transition process was another one. The deficit was $2.2 billion. And public authorities' debts with the Government Development Bank was even worse, $4.3 billion. To tell you the truth, January 2013 I was about to ask for a vote recount. (Laughter) But the law in

Puerto Rico does not allow the winner to request a recount. (Laughter) I was about to call my predecessor asking him to ask for a recount. The (inaudible) alliance has noted that in facing these issues states have become individual laboratories where (inaudible) experience are happening on many of these pressing issues. We address similar challenges and we need to learn from each other what works, what does not, and why, about errors and achievements, about how to reduce the former and replicate the latter. In many ways Puerto Rico's crisis simply suggests that because of its smaller and simpler economy it is only ahead of the curve, the curve that looms to many other states and municipalities. We have been forced to try tools that have not been tried before. We have had to knock on doors that other jurisdictions may need to approach in the not too distant future. We assessed the magnitude of the crisis that was over us, possible solutions were on the table, thus Puerto Rico will not rely on the same tools available for the States.

My administration acted swiftly. Puerto Rico adopted strong austerity measures. The island's budget had been cut by billions during my term, expenditures had been cut from $11.9 billion in 2012 to $9.1 billion today. We present to the legislature a value added tax alternative that will have imposed a more equal taxation system, but ultimately the bill that passed raised the sales tax to the highest in the United States. The public payroll had been reduced dramatically through attrition. We have deferred other obligations, we have withheld tax reforms, payables to suppliers have also been stretched to over $2 billion. The inability to our suppliers has resulted in the loss of commercial credit and many services will now be paid on delivery. Without supplier credit medication and public hospitals and air ambulance services to trauma centers were put in jeopardy. These emergency measures are unsustainable, harm our economy, reduce revenue, and diminish our capacity to repay our debts. Puerto Rico will not endure any more austerity.

In order to generate a permanent fix to the debt crisis, and lacking the mechanism that New York and Detroit had, we responded creating our own restructuring status. A federal court closed that door. We tried negotiating a voluntary settlement with the creators, but to no avail. We were pushed to the edge of the cliff. Puerto Rico municipalities and the island itself cannot declare bankruptcy. That's not a political statement, that's the law. The federal court decided Puerto Rico cannot restructure its debt under a court supervised plan similar to the Chapter 9 bankruptcy that U.S. cities like Detroit can access.

Imagine New York case without federal bankruptcy available. Imagine Detroit without the federal court. Puerto Rico was alone. Puerto Rico had no protection. Therefore, the crisis only aggravated through several years without Puerto Rico being able to act.

On July 1, 2016, two weeks ago, Puerto Rico was going to default around $1 billion in general obligation bonds. The island's senior credit protected by a constitution pledge on revenues. Creators and bond insurers have initiated multiple lawsuits, hedge funds filed an injunction before the Southern District of New York claiming the -- and I quote -- "absolute highest priority" over government resources, including those needed to provide essential public services. That complaint stated that in time of scarcity bond holders shall be paid before essential services. That is why we sought the support of Congress. Their response was PROMESA. PROMESA is a mixed bag. On one hand it provides the tools needed to protect the people of Puerto Rico from disorderly collection actions. The immediate stay granted by the bill on all litigation is of the utmost importance at this moment. Moreover, the authority to adjust our debt provides the legal tools to complete the wholesome restructuring fair to everyone and begin Puerto Rico's rehabilitation.

On the other hand, PROMESA has its downside. It creates an oversight board that unnecessarily undercuts the democratic institution of the Commonwealth of Puerto Rico. But confronting the upside and the downside of the bill it gave Puerto Rico no true choice at this point in time. So I needed to choose, misery for my people or unnecessary intervention from the federal government with our democratic institutions. When someone points at you with a weapon and asks you for your wallet you may say no, but the consequences are worse than those of losing it. Now it is time to regain the way to grow.

Throughout this process we have always made sure to keep the lights on literally and figuratively. Austerity is a very difficult pill to swallow, but taking emergency measures early on worked. Crime rate is half of 2011, unemployment rate has been driven down from 14.6, in 2012 to 11.7 right now, in a percentage base of course. Now we are ready for the balanced approach that will stimulate the economy while paving a path to recovery.

Now, our administration plans to use the tools provided by PROMESA and to prepare a fiscal plan that ensures that we adequately fund our pension funds and returns us to a sustainable debt structure. These steps will protect our most vulnerable citizens and help ensure a return to economic sustainability. The challenges are not over and prosperity won't return overnight, but our plans promise a bright future.

As you all know, in order to focus exclusively -- now it shows I'm the first governor that just stayed in Puerto Rico and not came to the States to college (laughter) -- as you all know, in order to focus exclusively on these crucial matters, I decided not seek reelection. Therefore, I can say that I will use my remaining time in office making use of the tools provided by PROMESA to develop a fiscal plan that is faithful to the best interest of the people of Puerto Rico. At the end of the day it was a crisis two decades in the making. It was not developed overnight and it will not be fixed overnight. I ran and was elected with the hope of being a two-term governor. But deciding to unveil the crisis, to show it to the world, and balancing the budget with no deficit financing, took me to a different path. It was scary. It was very scary at the beginning. And we can choose to freeze when we are scared. We can choose just to take the easy way out or we can choose to fight, to pursue our goals. We can choose to decide where we really want. I know we are on the right path to restructure our debt, to recovery and growth.

Thank you for having me here. It's always a pleasure to speak of lessons learned in the process.

Thank you, David. (Applause)

MR. WESSEL: Pro. You've done this before.

GOVERNOR PADILLA: Practice.

MR. WESSEL: Yeah. Well, it will be good in your next career.

GOVERNOR PADILLA: Yes. I don't know, maybe.

MR. WESSEL: Saturday Night Live maybe?

GOVERNOR PADILLA: Could be. (Laughter) Jimmy Fallon?

MR. WESSEL: Yeah. I hear it pays well.

GOVERNOR PADILLA: I sing very bad. I cannot do what the president did with him, you know. Orange is not the new black and stuff like that, I cannot do that. Not good rhythm.

MR. WESSEL: Yeah, the President is unusual in that respect.

GOVERNOR PADILLA: Yes. (Laughter)

MR. WESSEL: So, you know, if I were sitting here with you, governor, as a young Puerto Rican man, say a 30-year-old man, educated, and I told you I love Puerto Rico, my roots are here, but I really don't see a future for me here. I see decades of belt tightening in the government, deterioration of public services, we won't even have control over our own destiny because we'll have this control board. I'm thinking of leaving for Nueva York, or maybe Chicago. Would you tell me I'm making a mistake? And if you were trying to convince me to stay what would you tell me?

GOVERNOR PADILLA: Well, first I will suggest not turn on CNN (laughter) or FOX or at least choose Dallas or Minnesota right now. Isn't fair with those jurisdictions that have great things and have just been through a crisis and I empathize with them. But as New York is not what we know or what is not occupy Wall Street, and Dallas is not the shootings. So Puerto Rico is not only the fiscal crisis. Right now in Puerto Rico, Puerto Rico per square mile is the best -- is number one drug producers -- pharma producers in the world. Seven out of the ten (inaudible) pharma products in the world are manufactured in Puerto Rico, seven out of ten, including number one, that is Humira. Twelve out of the 20 (inaudible) medical devices manufactured in the world are manufactured in Puerto Rico. So there's a lot of opportunities, but we need to fight this crisis out. And what will happen at the end of the road, why I choose not to continue that -- can we go to the --

MR. WESSEL: Upward path of the debt.

GOVERNOR PADILLA: Yes, upward path of the debt, what happened in New York after the board, what is happening in Detroit, what happened in D.C., what happened here? So the change was -- I remember the first time I came to D.C. it was 1993 if I remember when I was a student in the University of Puerto Rico, and there were just a few blocks around the mall that it was safe to walk. But it's now different. So Puerto Rico will be different. Even though right now in Puerto Rico you have less crime than four years ago, less unemployment rate than four years ago, yes, you're right, there is diminishing in public services because we have an issue of liquidity and an issue of burden of debt. But that will be fixed. So it's now a moment of opportunities. It's precisely a moment of opportunity.

I just want you to take a look at that graphic because for the first time in history debt is going down. And that does not include the restructuring of the power authority. So you will have to reduce $9 billion more to the last column. So it will be even lower very shortly.

So where we are moving is where I think we should be moving.

MR. WESSEL: So let's talk about where we are now. PROMESA passed about two weeks ago, you put forward a fiscal plan. Are you going to radically change that or how are you going to change it as part of the PROMESA process?

GOVERNOR PADILLA: The articles of PROMESA the request the government of Puerto Rico to a new fiscal plan, or they say a fiscal plan, were based on the fiscal plan that we put out last I think September or December of last year. So we complied already with most of the demands on the new law. But we are now working with that fiscal plan to amend it. It will be dramatic changes within the plan. So it will be areas where we'll be adding to the request that the government needs to make to itself, but at the same time softening in other areas. For example, I think that -- and the government shall be more efficient and that needs to -- a reengineering of the government without firing public employees. I already presented bills to reduce 24 agencies that haven't passed. We need to take a look at that again, to include that in the fiscal plan. But the other side, we need to protect the University of Puerto Rico. The University of Puerto Rico is an investment, it's not a cost, it's not a burden. It's the principal engineering, bilingual engineer center in the United States. NASA or Honeywell recruits more people, more engineers every year from the University of Puerto Rico than from any other university of the United States. So we need to protect the University of Puerto Rico as a real tool to our economic development. And that has to be protected in the fiscal plan.

MR. WESSEL: So the fiscal plan will be same shape and size, but just reallocating some of the numbers?

GOVERNOR PADILLA: There will be some changes in the size, but the (inaudible) will be in it.

MR. WESSEL: I see. And since PROMESA passed have you had any invitations from the creditors to sit down and start talking under the new arrangements?

GOVERNOR PADILLA: Not directly. Maybe through the government bank. But prior to PROMESA they approached directly to me and I was able -- I think it was July 22 -- 21 -- that we were about to have a meeting in New York --

MR. WESSEL: June 21.

GOVERNOR PADILLA: June -- June, you're right. And they cancelled. I don't know why. I don't know if they were waiting to PROMESA not to pass so they will have more leverage after July 1, but PROMESA passed. And I think it was Marco Aurelio, the emperor, who says the conquered have the right to know they have been conquered. They lost, they lobby, they spend a lot in the Hill, they spend a lot on -- some of them spend a lot on ads, lying about Puerto Rico, lying about me. Some of those are even I liked. (Laughter) You know, there was one full page, I think it was the The Wall Street Journal, I don't remember, that it was Cristina Kirchner and I. You know she was the president of Argentina; I was the governor of Puerto Rico. (Laughter) So, you know, comparing me with Cristina Kirchner, you know, they have -- messy and stuff like that. (Laughter) So I liked that one. I do not like the Maduro one, but, you know, fair, fair. (Laughter)

MR. WESSEL: You've got to take the good with the bad.

GOVERNOR PADILLA: The good and the bad.

MR. WESSEL: So when you look at the fiscal situation in Puerto Rico --

GOVERNOR PADILLA: So for them to know that they spend a lot and I laugh. (Laughter)

MR. WESSEL: Good, good. Do you think Puerto Rico has reached the limit on what it can effectively raise in tax revenue? I mean you pointed out you proposed a VAT that was going to partly reduce the income tax. The legislature rejected it, you ended up with an 11 percent sales tax.

GOVERNOR PADILLA: 11.5, yes.

MR. WESSEL: 11.5 percent sales tax. Is this it for what the Puerto Rican economy can produce revenue, tax revenue?

GOVERNOR PADILLA: Income tax goes against the productivity of the person, is bad for the productivity of the person because you are penalizing someone because he produced. Value added tax is where the rest of the world is moving. During the 1960s only five countries in the world have a value added tax. Right now 160 out of 190 countries in the world have the value added tax. Of the 20 biggest economies in the world, 19 already moved to the value added tax. Only the United States remains. So it will happen and I think it's the right way to go and I think that Puerto Rico should move, I think the United States should move into that direction. It will happen. It's like legalization of marijuana. It will happen. (Laughter) Earlier, sooner --

MR. WESSEL: I'm pretty sure both the legalization of marijuana and the value added tax have been discussed on this stage, but never in the same sentence. (Laughter)

GOVERNOR PADILLA: Welcome to Puerto Rico.

MR. WESSEL: But is the level of tax -- is this it, have you squeezed all the revenue you can out of the Puerto Rican economy?

GOVERNOR PADILLA: I think that we were -- in words of experts like Jack Lew or Ann Krueger, former economist of the IMF, International Monetary Fund, sometimes we went too far. So the austerity measures and -- we went -- we cannot have the burden anymore. We need to make economic growth. If not, we will enter in that debt spiral. Rising taxes today will allow us to have more money today but less tomorrow, then we will have to raise taxes even more next week because we get into that spiral. And I think we need to move out of that spiral.

MR. WESSEL: And will your successor as governor run into political obstacles if he wants to reduce the size of the public sector more? I mean you have fewer people but you still have more teachers, you have more prisons.

GOVERNOR PADILLA: Well, the discussion is changing now in Puerto Rico because everybody found out that we have inefficient government that is not big on the number of employees, but of the size of the structure of the government that is inefficient. When I was sworn in it was 105,000, it's right now 89, only through attrition. So what we need to do is to move those public workers where we need them. We have a lot of people in some agencies doing not that much and we need them -- for example, right now I have like 1000 police officers doing administrative jobs in the police department. So we have been moving. We already moved 300 people from the Department of Education to the police department so we were able to put more policemen and women in the street. So that's we need to reengineer the government.

MR. WESSEL: Finally, before I turn to the audience, are there savings realistically available from the pension system? You did the pension form of the ERS, you tried something with the teachers, the court said you couldn't do it. Is there more to come from the pension system or is that --

GOVERNOR PADILLA: It's something that amazed even to republicans in the Hill is that we were able to change the main pension system in Puerto Rico from defined benefit to a defined contribution including actual workers, which was the different task. I invested a lot of political capital on that because it was the right thing. Where's the problem right now? That is underfunded, is $.07 to dollar $1.00. So for each $1.00 that goes out only $.07 goes in because government hasn't been able to put in their share into that account. So what we need is to fund the pensions systems.

Something that I didn't mention in my remarks is that when I was sworn in the debt ratio to the budget was -- and last month -- was 36 percent. The state with the highest debt service ratio to budget is Hawaii with 13. So we have almost 3 times. The average in the States is 5 percent. The average in the world is 7 percent. So 36 is humongous, is something that no one can handle. That's why I said more than a year ago that the debt is unsustainable, that we cannot pay, that we need to restructure.

MR. WESSEL: Okay. We have a lot of people here; we'll take some questions.

Natalie, I'll start with you here. And for the governor's benefit would you identify yourself?

MS. COHEN: Natalie Cohen with Wells Fargo Securities. Thank you very much for your presentation. There's a great deal of opposition to PROMESA. The candidates running for governor have publicly opposed it, CNE came out and spoke against it. I don't have any idea what the man on the street is thinking. I'm thinking maybe there's a different perception. But could you look into the crystal ball a little bit and say perhaps how will this go forward without some kind of buy in or support or the island?

GOVERNOR PADILLA: I will try to do it in the same order that you pointed out. That's why I choose not to run. (Laughter) I understand them. There's no federal law that goes too much into our democratic institutions. And I do not like that. But again, not thinking about November, but thinking about paving the way, and I say it as I feel it. It's like when someone points at you with a gun and asks you for your wallet. I may say no. No we will not surrender our democratic institutions. Then there will be misery to our people. Creators make a huge mistake with the injunction that the request from the Southern District of New York, the federal court, because they said that the governor -- they said to the court that the governor was saying publicly that he will pay essential services prior to pay them. Hell yes, that's my job. So I went to Congress in the final days and said, you know what, this is what will happen, and if that judge grants that injunction they will put an embargo, they will apply the injunction to our treasury accounts, so I will not be able to provide essential services. And even though that they do not want to say it publicly, I have a feeling -- I cannot talk about them, I cannot, you know, speak for them, but the candidates know that they have to deal with that. The candidate from my party, Dr. David Bernier, he already said, you know, it's approved, we have to deal with it, let's work, let's make it happen, and let's make it the least that is possible. So I think that's the right approach. It's approved, let's reduce our debt.

What in the streets? The main newspaper recently presented a poll that shows 54/46 against it. So it's almost half and half. For me, I have three children. When they grow up Puerto Rico will have less debt than today. That will fulfill myself.

MR. WESSEL: On the aisle here. I know your last name, but I don't know your first.

MS. TER-MINASSIAN: Teresa Ter-Minassian from the IMF. First of all, thank you very much for a heartfelt presentation.

My question is what will be the motives of growth for Puerto Rico going forward?

GOVERNOR PADILLA: I'm sorry, the?

MS. TER-MINASSIAN: The motives of growth.

MR. WESSEL: The motives of growth.

GOVERNOR PADILLA: Okay, thank you.

MS. TER-MINASSIAN: Can you be a bit more specific? You have indicated something, but can you be a bit more specific as how can -- Puerto Rico cannot get out really of, you know, debt spiral unless it starts to grow. So what are going to be the actions, the policy actions the government can take, what can the international community do to help Puerto Rico regain growth?

Thank you.

GOVERNOR PADILLA: Thank you. Thank you. And I don't want to forget the last part of the question about the international community because yes, there is something that the international community can do.

First, the two main approaches to economic growth come from the administration here in the States and from Congress. The administration's approach goes to Medicare and Medicaid, that we allowed Puerto Rico to have -- I'm talking about parity. Medicare is obvious because we pay the same but receive less. That will allow Puerto Rico to have -- if I remember well $6-7 billion more a year. The Congress approach is more through economic incentives to corporations like 936. When I say "like" it's not that much, it's in that approach. I think we need both. So we need to bring those companies back because we'll put into production the best part of us, that is our skilled workers. So if you ask Lufthansa why they have the only MRO of their own in the hemisphere in Puerto Rico they will say skilled hand workers. If you ask Amgen what the biopharma -- the biggest biopharma building in the work is in Juncos, Puerto Rico by Amgen, they will say skilled hand workers.

Second reason, taxes, but first one skilled hand workers. And of course our healthcare system is a priority, so we will have a lot of help with Medicare and Medicaid. So those are I think the main goals right now.

About the international community, recently I went to the United Nations and demanded from the United Nations to request the United States to comply what the United States addressed to the United Nations in 1953 when they, the United States, stated that Puerto Rico achieved self-government enough not to be part of the list of territories that need colonization. The bad side of PROMESA that I point out mess with that. So the United States needs to re-enter in that dialogue with the people of Puerto Rico so we can achieve again the autonomy level that allowed us not to be a colony. I think that it's not where the United States wants to be with the issue that the United States has with the rest of the world, to have a colony of their own.

MR. WESSEL: Harry? I have two different sets of times. Do we have time for another question? Are we okay? Okay. Nick?

MS. LONG: Cate Long. Thank you, Governor.

MR. WESSEL: Wait, Nick Timiraos in the back.

MR. TIMIRAOS: Thanks, David. Nick Timiraos of The Wall Street Journal. Governor, I wonder if there were specific steps that you were unable to politically get through the legislature over the past three and a half years that now, whether it's labor law or other kind of economic competitiveness steps addressing overcapacity in the public sector, that you would now ask the oversight board to implement maybe with some of that political constraint being removed by the federal legislation?

GOVERNOR PADILLA: Thank you. And I think it's a very good question, but I think what will happen is we will be able to do it. Remember that PROMESA or the board will have a say if we do not do it ourselves. So if we do not act in a responsible way. For example, people say, you know, the board will be able to approve a budget. That's true only if we are not able to approve a balanced budget. So PROMESA, the board, the oversight board will not deal with our budget if we do it the right way. As I pointed out before we need to consolidate agencies in Puerto Rico, not to reduce public workers. I do not agree with reducing public workers more than we have been able to do through attrition. But we need to make the government more efficient.

You know we have, for example, what we call (speaking foreign language). It's like ombudsman, but we have the ombudsman, then we have the (speaking foreign language), the ombudsman, the ombudswoman, for the women and for elders, and for sick people (speaking foreign language). So my mother, she's a woman, she sometimes thinks -- she doesn't want me to say it, but she's an elder (laughter) -- and she can go to the ombudsman too. So we propose create like in the rest of the world it's happening, create one, just one place. It doesn't pass. We need to do more. I think it was 2013, September or October 2013, if not it was 2014, that when it was this -- when you guys were discussing here if the government needs to raise the gas tax, we did it. So we're paying now the half for the gas in the pump, but we have more tax from it. But it was approved -- it delayed too much, so we weren't able to go to the market and take part of the debt from the Government Development Bank to add liquidity to the bank, not to add more debt, but to add liquidity to the bank and to negotiate that debt. But we were unable to do it because we delayed too much. Now we will need to be more efficient in the way we deal with those problems, to give you just two examples. And the budget needs to be balanced always, not sometimes.

MR. WESSEL: Steve. Steve, can you stands up so (inaudible) can see you. And then there's a gentleman behind whose hand I see but I can't see who it is.

MR. WINTERSTEIN: I'm curious about --

MR. WESSEL: Could you identify yourself.

MR. WINTERSTEIN: I'm sorry. Steve Winterstein with Wilmington Trust. I'm curious, your perspective on the improved U.S. relationship with Cuba and what's the effect on the island and --

GOVERNOR PADILLA: I just visit them. I'm the first sitting governor to visit Cuba. Cuba and Puerto Rico have a lot in common, not only because we are part Caribbean Islands, our histories -- you see the flags are the same in (inaudible) the colors. They were both created in New York at the same time and (laughter) -- yes -- and the revolutionary party of Cuba was founded for the independence of Cuba and Puerto Rico. Our civil code is the same. Of course property law is a little bit different. (Laughter) But we have a lot in common.

Cuba will be a formidable competitor, but it's not right now, and it will take a little bit for them to be. It will happen and as governor, as Puerto Rican, and as a Latino, it's something that cannot bother me. I'm happy for that. Good. Good for them and good for everybody. I think that if Cuba opens and there's more opportunities for Cubans that's good. They will compete, we will compete. That's part of the game. And we will need to win and they will try to do it. (Laughter) So let's make it happen. I'm happy. I'm very happy. I visited them. I'm planning to open an opportunities office there, interest for doing business office in Havana and already in conversation to do that. So it's something that is good. I'm so glad that is finally happening. And I will tell you, if you agree or disagree with their revolution in Cuba and with Castro's government, that's to decide. The embargo is bad no matter if you agree or disagree. It's bad if you agree with Cuban government because it's unfair. Why they cannot do business and commerce with whoever they want, whatever they want, and whichever they want to do commerce with them. Why the America people cannot do business with them? Because they are communists? Well, Chinese are too and I think that -- I don't know how many of the pieces that we are wearing here are made in China (laughter), beginning with myself. But if you're against Castro, against the revolution, then you are giving them the perfect reason for them to unite the people against the embargo. You know, if there's a lack of anything you can blame the embargo. So if you agree with them it's unfair, if you want them to be changed, you are giving them reasons to stay.

MR. WESSEL: There's a gentleman --

GOVERNOR PADILLA: Dominicans are very good too. (Laughter)

MR. WESSEL: Rich.

MR. CICCARONE: Richard Ciccarone, Merritt Research. Governor, you know, this is a fiscal tragedy and we're at a municipal finance conference. I like the way you started off and said where have we been, how did we get here. But that's also begging the question to take a look at where mistakes were made along the way.

If we could fantasize and say we want to do time travel and go back in time and say what would we do it differently, when we would have done it, we might both agree about Section 936 shouldn't have been turned off when it was turned off because in the midst of the recession. But one of the things that I think has been a criticism in the municipal bond market, both within the market and players and also critics of the market, is that the market enabled the situation to happen. And I'm curious to say would we all have been better off -- you would have been better off if the market would have -- because the fundamentals were already out of line in 2006 in terms of debt levels even then, but it went up and exploded -- would Puerto Rico have been better off to go against the pleading that came from the government to buy the bonds, just not to have bought the bonds.

GOVERNOR PADILLA: If I get well the question, if not please go back. We go back in time, 1984 when Puerto Rico was removed from the bankruptcy code, or 1996 when the 936 was eliminated, and 2006 when we got into recession, but filled the gap on the reduction of wealth creation with loans. And the government of Puerto Rico knew it, but they decided to keep it hidden from the people just to make people not to feel. And the market knew it too, and standard and poor knew it, and (inaudible) knew it and feds, they knew it too. But Puerto Rico kept borrowing and the market kept providing the money. And the debt was rising and those numbers were public and everybody said that the debt service ratio to budget was rising too, but no one said anything. So it comes to the end. It's just happened. So it's an issue of responsibility on both sides. Let's say two ways, Congress and the United States, the market and the government of Puerto Rico. I think that it's a shared responsibility and those numbers were public. Nothing is hidden there.

MR. WESSEL: Okay. There's a woman in the back there.

GOVERNOR PADILLA: Cate Long.

MR. WESSEL: I'm sorry.

MS. LONG: Hello, governor, it's Cate Long, Puerto Rico Clearing.

GOVERNOR PADILLA: Hi, nice to see you again.

MS. LONG: Two things.

MR. WESSEL: Cate, for those of us who don't know you, who are you?

MS. LONG: Cate Long, Puerto Rico Clearinghouse. I do research for bond holders.

My first question is the Puerto Rican legislature sent you HR 2959 to create a debt service fund in the fiscal 2017 budget of $450 million. Do you plan to sign that bill?

GOVERNOR PADILLA: I arrived last night here and called back every two hours, let's say, and it just arrived from the legislature so I haven't read it. And now, I don't know if here in the States it's the same, we have 30 days since it arrived. So I ask memorandums from agencies and decided what signed or vetoed. What happened with 2959, in Puerto Rico the session ends on June 30. But the last date to approve deals in both houses, in both chambers, the House and the Senate, is five days earlier, 25. And there were bills that weren't able to be approved by both chambers, even with amendments. So they are in conference. So what they did is that they put a lot of bills in that one, so they amend the 2959 to include other issues that weren't able to pass by June 25. So it's a bill about a lot of things, that's why we need to study it before deciding to sign it or to veto it.

MS. LONG: Thank you very much. The other question would be in your term you issued the largest junk municipal debt bond in the history of the United States, the March 2014 GO.

GOVERNOR PADILLA: '14.

MS. LONG: Did you see the problems that lie ahead and the possibility that 15 months later you say you need to default on that debt?

GOVERNOR PADILLA: Well, things didn't come out as we were thinking that they will come out. It was funny because we did everything right and the credit agency, for example, said you know that's -- what the line they use is like credit positive, but whatever, another reason. Sometimes they are moody, sometimes they are standard, sometimes they are poor, sometimes they are (inaudible), you know. (Laughter) And so you need to fix retirement funds. We did it. Not great positive, but we will downgrade you for another reason. So we went there and worked for the other reason and we fixed it. Not credit positive, but -- and they kept it that way. So the market closed. And I was able to borrow at 12 percent. I was able to do it again and continue the path and drag that 70 to 90, but I said no, you know what, not anymore. So I decided to go the other way and Cate is right, but things unveil after in the opposite way that we thought it will happen.

MR. WESSEL: So do you wish you hadn't done that last borrowing?

GOVERNOR PADILLA: I think that we will be -- if -- with a crystal ball as she said --

MR. WESSEL: Right.

GOVERNOR PADILLA: From Wells Fargo, right?

MR. WESSEL: Right.

GOVERNOR PADILLA: Knowing now what I knew -- what I know, if I --

MR. WESSEL: Right. If you knew now what you --

GOVERNOR PADILLA: Maybe no.

MR. WESSEL: Maybe not. Okay.

GOVERNOR PADILLA: But knowing then what I know now.

MR. WESSEL: Right, got it. Right.

GOVERNOR PADILLA: I would like to go senior year in high school (laughing) knowing what I know now.

MR. WESSEL: We got the idea. (Applause) Governor, thank you very much for your time and your candor and your sense of humor. I admire someone in a job like yours who still has a sense of humor. I hope you can keep it for the next six months.

GOVERNOR PADILLA: Let me tell you, David, three and a half years ago I have the hair like his (laughter), now I have like yours. It can be worse.

MR. WESSEL: And pretty soon -- it could have been -- it could be Peter Orr's next, right? (Laughter) Okay. I'm going to let the governor go. If reporters want to continue the conversation it will be in the Summers room. And I'd like to invite the next panel up.

GOVERNOR PADILLA: I just wanted to say, what I said about CNN and FOX I have nothing against them. I see it every day. You know what, they don't say anything wrong about me. (Laughter)F So I prefer it.

MR. WESSEL: I see.

GOVERNOR PADILLA: Thank you.

MR. WESSEL: Okay. Thank you very much. (Applause) If I can get Natalie Cohen, Gerry Rosen, Jim Spiotto, and Ben Watkins up here we can reflect on what we just heard and what we've heard all day. Natalie?

MR. WESSEL: We have one more, I don't know where he is but we're going to start without him. Evan, maybe you can go out to the front and see if Louise can help you find Ben Watkins.

SPEAKER: He's here.

MR. WESSEL: He's here. I'm going to start and he can join us.

Just for people that-- uh, Natalie Cohen, many of you have already met, the senior analyst at Wells Fargo and one of the experts on municipal finance market.

Jim Spiotto, managing director of Chapman Strategic Advisors has also been involved in the business for a long time and here he is. On queue.

Judge Gerald Rosen is a former chief judge of the U.S. District Court for the Eastern District of Michigan who was a key player in the Detroit bankruptcy that's been mentioned repeatedly today. Some people said it's a model and some people say it's not.

And also we're very pleased to have Ben Watkins who is the director of the Division of Bond Finance in the state of Florida, a job he has held for how many years? Forever, right?

MR. WATKINS: A couple of decades.

MR. WESSEL: A couple of decades. Nothing much has changed in the municipal markets since then. (laughter)

So, what I thought we could do here is reflect a little bit on what we've heard today both from the governor and from others about whether the dynamics in the municipal markets in an era that we've lived through Detroit and we've lived through a Puerto Rico and I think we all know that wasn't the last instance of municipal distress that we'll go through. And I'd like to-- maybe I can start with you Judge Rosen.

I think during the day there have been a number of people who have observed that we have a set of laws that are supposed to deal with bankruptcy in the corporate and private sense. Chapter 9 is quite different and it's quite different for very good reasons that you can't- no creditor is going to get to cease the city hall and sell it and we expect municipalities to continue to provide services but on the same time there are questions of equity. How do we decide as the governor said he is kind of proud that-- the creditors said he was going to put essential services ahead of paying the bond owner. On the other hand, bond holders who have lend money to a jurisdiction have some reason to expect that that entity which can afford to pay them back will pay them back.

So, where are we in this balance and what has been changing?

JUDGE ROSEN: Well let me begin where you began Dave which is with the statute, the Chapter 9 statue and when I first got involved with Detroit I have to say I was surprised at how thin it was. It is really more aspirational and hopeful than it is a blueprint for moving a municipality forward out of bankruptcy. So-- but it does strike an importance balance not only between a city not being able to go out of business as a Chapter 11 debtor can do ultimately but between political leadership and democracy and the need for a robust restructuring under court supervision and if you look at Chapter 9 from a 30-thousand-foot view that's clearly what the-- that's clearly what the statue is trying to do.

In Detroit we were-- we had-- in addition to the overlay of the Chapter 9 stature we had an emergency manager. And there was a state statue that was provided. Very, very, robust power. Some would say robust power on steroids to the emergency manager and that gave us an opportunity to really not just restructure debt because-- what we had to do in Detroit was much more than simply restructure the debt. Detroit was service, delivery, and solvent. It really wasn't a city at all. I think most of you are familiar with the story of Detroit. But we had to provide a pathway forward out of bankruptcy on the other side so that the city could be a city again. I think one of the important things that was done to strike this balance as you talk about was to hold sacrosanct within the plan of adjustment. The 1.7 billion dollars in revitalization funding for light removal, hiring police, turning lights on-- 40 percent of the 90,000 street lights in Detroit were out, and to really rebuild the city and that process is strongly underway now.

But it is important I think for municipalities coming into a bankruptcy to look at what the city is going to look like on the other side of the bankruptcy and not simply think about, well how are we going to restructure debt. Because it's about-- for municipalities it's about much more than restructuring debt and striking that balance-- and now I'll get to the delicate question that you asked of striking the balance between the financial creditors who supplied funding over many-- in cases over decades, and employees of municipalities and their retirees. And that was definitely a tension we had to deal with and I know that some in the financial creditor community felt that we dealt roughly with the financial creditors and that the retirees were the disproportionate beneficiaries of that. I would argue that really wasn't exactly the case because the retiree debt consisted not only of the pensions which were approximately 3-and-a-half billion dollars underfunded depending on the discount rate that you used. Some say it was much more. But also the OPEB's. And if you look at the retiree's--

SPEAKER: Other post-em--

JUDGE ROSEN: Other post-employment benefits, sorry. The healthcare. The retirees took about a 90 percent reduction in their healthcare. It's true that we were able by bringing in about 870 million dollars in new money leveraging the art-- bringing in some state funding and some private funding, it's true that we were able to pretty much hold the retiree's harmless. The civilian retiree's took a bit of a hit, 4 ½ percent and lost their COA but if you look at the retiree's as a whole they took tremendous hit on their healthcare. We stood up some VEBA's which we're very hopeful will work but the quality of healthcare that these retirees are getting are not great.

MR. WESSEL: If you look at the world today, after Detroit, after Puerto Rico, after Harrisburg and compare it to where it was say, I don't know, 20 years ago, I don't know what the right thing is. Is something really different? Rich made the point this morning, and I've heard this phrase a lot, that we've gone from capacity to pay to willingness to pay. Has there been some C change?

SPEAKER: I think that's a fair question. If we've had a C change that creates a real issue in the credit market. But I think the one thing that we see happen to the good is more and more the papers indicate, the PEW paper and the paper from USC Dermont paper and basically we have developed a number of different ways, and some uniquely by state, to monitor the problem and to address it because Chapter 9 was never intended to be: I have a problem so I'm going to Chapter 9. Chapter 9 was the last resort. And in effect-- one of the reasons when Chapter 9 first came out the people who argued strongest for Chapter 9, civic and politic in the-- before Congress was the city of Detroit. I think they were clairvoyant to 2013, but the reason why the wanted it, they had a composition of creditors and they had a holdout. Ninety-two percent signed up and 8 percent said, we won't do it. And they used Chapter 9's passage-- and a number of other cities did too at the time, to convince the 8 percent, you really don't want to go there.

And so I think that-- one of the things that the market can't understand, it may not be happy over it but cannot understand unwillingness to pay but inability to pay, the market has historically understood that. The market has historically has dealt with those situation and you may have-- you may be a creditor with all the rights in the world to everything but if you don't help the municipality help itself, i.e. have it continue and grow you're not going to get paid. Many times I remember as a recovering lawyer explaining sometimes to the client, now we can establish this legal principal or you can get paid. [laughter]

SPEAKER: You can't beat principals.

SPEAKER: Right. I mean, I think that that's important and I think what we've learned now in the monitoring and from these experiences, we need to be quicker and firmer on how we address things. Some states do that; they don't have as many problems. Many don't even have any problems and that-- by that I mean not only just do you balance your budget, what are your pension issues, and that longer term obligations that have to be paid today but you better have a good plan on how to do it that is sustainable and affordable.

What about infrastructure and business development? I think you're going to see a trend in the states going forward for legislation to make sure they have the infrastructure. We have sort of forgotten about infrastructure in the last 8 to 10 years and I think there is a real need for that. That can stimulate the economy.

Business development. I think you're going to see-- one of the things the legislature seems very concerned about, how can I get more jobs back to my state. When I've talked to legislators in their conferences they are interested in two things: How do I lower my borrowing quest which is really a perception of less risk; and second, how do I increase my economic stimulus, my jobs and growth because what is insolvency in a municipal sense. And as I tell people, I'm not over weight I'm just too short for my weight. So, that's the same thing with the municipality. They don't have enough revenue. How do you create revenue? You know, raising taxes, lowering services is a good way to have people leave. Some coming up with a good plan and I think that's what the challenge for the future is and I think that unwillingness to pay hopefully is a momentary flight of fancy and it's really the inability and I think as long as it's inability the markets and the municipalities and legislature will find ways of dealing with it.

SPEAKER: So this is coming from a guy from Illinois with a year in to with no spending plan. In all seriousness--

SPEAKER: Do as I say not as I do.

SPEAKER: In all seriousness, in Illinois--

SPEAKER: He's not the guy you--

MR. WATKINS: No, but he is refereeing to a rational and logical plan--

SPEAKER: Right.

MR. WATKINS: -- so-- and government at the same time. Jeb and I happen to agree to reinforce what he is talking about and that is bankruptcy in the state of Florida is-- represents a failure. We simply don't go there. That's the policy-- the governor if the gatekeeper and it's been a long standing policy that it's not an option and there was a great session this morning, PEW, (inaudible) and Gail Sussman did a great job this morning talking about the systems in place for monitoring and identifying deteriorating fiscal situations before they get to the point of being unmanageable. And I think that's absolutely a critical element to the solutions to avoid the problems that we've encountered in Detroit and Puerto Rico. So, there's a lot to be learned from that perspective.

MR. WATKINS: So, in Florida-- is there an instance where this monitor picked up a problem and you solved it before it became a--

MR. WATKINS: There have been a-- so we are according to PEW we're one of the active but not the very most active, but anyway, there is a statutory framework in place that has a number of additia that gets reviewed annually and then gets investigated if there is anything that is out of kilter and then there are a range of different powers and tools that can be implemented that can address those.

Probably the most intrusive is the creation of an over-side board and that's occurred three times in my recollection and that's in the local government area so that was the city of Miami say 15 years ago and it's currently with the city of Opalaka which is a smaller jurisdiction in the same area and it of course involves creating an oversight board to make the politically difficult decisions that the elected officials apparently can't make. And in those set of circumstance that we-- and we're a fiscally conservative state with the Republicans in the House and the Senate as well as statewide elected offices so what quickly becomes apparent is state oversight doesn't mean a check. What it means is experts and technical resources to get it right because-- I mean we live in Florida, even the grass grows in the winter time so we're not confronted with the situation where we have organic deterioration in an economy. The set of circumstances that we've always dealt with is just-- you're playing garden variety mismanagement and the inability to make difficult decisions financially and getting out of balance and having that perpetuate itself and then that manifests itself so it's normally technical expertise and budgeting, revenue estimating, setting up the appropriate funds and accounts. The normal blocking and tackling that keeps governments running on an even keel.

MR. WESSEL: Natalie, this morning Dan Bergstresser showed us that holdings of municipal bonds are increasingly concentrated in a small and-- really high wealth individuals. We've had cases like Detroit or the stuff that's put into the law in Permasa that clearly are trying to tip the balance a little bit, depending on your perspective to much or too little, do you-- from the point of view of the investors, the municipal buying investors you talk to, do they worry about this-- that increasingly it's going to be socially acceptable not to pay off your municipal debt the way it became socially acceptable not to pay off your mortgage during the financial crisis.

MS. COHN: Right. A couple of responses to that. Clearly investors are worried about the issue of pensions versus debt, that's the big question. And what the priority is what the priority would be in a workout situation. That's clearly playing out and played out in Detroit and in Puerto Rico and will likely play out in a number of other places where bondholders and underfunded pensions come to the fore.

The other thing, and I'm glad Judge Rosen you started with this that I find a little curious and I'm not quite sure what to do with it, is the issue of service delivery and solvency. I'm not an attorney but my understanding of Chapter 9 is that it's silent on that aspect completely. You have to be a municipality, you have to negotiate in good faith and you have to be insolvent from a financial perspective not from a service perspective and this terminology has crept into the Chapter 9 discussions.

I certainly understand the concept and as a credit on the list I look at it, but I don't know how it will then play into decision making in recoveries. The other thing that I'd really like to bring up, and this was brought up in the panels this morning and I find a little bit difficult to process is the value of the dollar is becoming whose dollar it is that they invested. And that came up this morning, it's certainly playing out in Puerto Rico in terms of the press against hedge funds against vulture investors which I may add includes a Supreme Court justice who recused himself from one of the high court's cases. Not everyone who is invested in Puerto Rico is a vulture or a hedge fund and what is happening in Chapter 9 is that the value of that investment, or who has made it is becoming more prevent and I don't remember her name but she was bringing up the point that in Chapter 9 or in some of the workouts in municipal bankruptcy that certain investors are being punished and being punished for being those bad guys that invested their money.

So I'm not expressing any opinion on whose value judgment or whose better or not but in Chapter 11 I'm going to guess that that is not an issue, and that did come out this morning, that's certainly something that the investment community actively is wrestling with.

MR. WESSEL: So you mean-- so if the result of all this is that some municipality is in distress and their bonds are trading at 30 cents on the dollar and you buy them at 30 cents on the dollar and then someone like Judge Rosen is trying to weight the equities between the retirees, the services, and the bond holders-- are you suggesting that it's not relevant that hedge fund bought the stuff for 30 cents on the dollar to decide if you want to pay 42 or 44 cents on the thing. It shouldn't be a criteria? Or are you saying that-- I mean--

MS. COHEN: I'm saying that the law itself should be indifferent as to where the money came from but the recovery should be fair across all classes. And maybe it's more in the press than it is in the courtroom but the press is clearly identifying certain investors over other investors. If a mom and pop investor, you know, an individual family bond holder you're not looking to see if he is a wife beater or a child beater, is he a bad person and he's putting his money into Puerto Rico or Detroit or Harrisburg or wherever, you're not judging that person or that institution for who they are. That's all I'm saying about it. I'm not talking about the legal aspect of it.

MR. WESSEL: I'm going to get more of the audience involved in a moment because we have so many good people in the audience as well as on the stage. One of the things that I'm puzzled about, so what is this period of very low interest rates do here. On the one hand it makes it cheaper to borrow and I've learned that this morning-- earlier today that you borrow you can refinance your municipal debt and there are funny people to help you do it and (laughter) on the other hand it makes all your pension liabilities look horrible, right?

So what is this period of very low interest rates and the prospect that rates are going to be lower than normal for a long time due to this whole picture.

SPEAKER: Well, you know, you really hope that you don't fall into the situation of never missing an opportunity to miss an opportunity. By that I mean I think during this period of time we haven't yet but we should have been doing all the borrowing from infrastructure, all the borrowing for stimulation of our economy but we haven't. But that's water over the dam.

SPEAKER: It's not too late.

SPEAKER: Yeah, I do think though there are some sort of principals, I mean, sort of playing out against what Natalie said. I do think the bankruptcy code one was always intended to be a last resort. It does have in it sort of the principals of how this works because the state and the federal government of (inaudible) soverance (sic) it's not the federal policy on what the priorities are. There's a section that's called 903 that basically says that if the state passes legislation that controls how a municipalities exercises its governmental powers including its expenditures the bankruptcy code can't-- (inaudible). If-- the bankruptcy court doesn't have any jurisdiction over the revenue property or political affairs or enjoyment of income producing property unless they municipality consents and the municipality as a sub-sovereign of the state can't consent contrary to state law. So I think that part of this question of-- the law professor, Juliet, who questioned what are the priorities, I think that there is pregnant in there the ability to, as I think Bart was talking about, set priorities by state legislation which will help address the service insolvency because the one thing that-- what's in the best interest of creditors, people read that and say, well I'm supposed to be paid in full. That's in my best interest. No, I think what Congress meant and what I think it's interpreted as some to be is that you have to be sustainable and affordable. You only get paid to the degree that the municipality has an ability to pay. And if you're not providing essential services and infrastructure people move out, (inaudible).

SPEAKER: Right.

SPEAKER: And so I think the low interest rates is still an opportunity, who knows when that will end, and we ought to use it now both by legislation to encourage it, setting up priorities to encourage that we don't end up with this insolvency, and use that because again Chapter 9 is a last resort. It also is the big fear of the market.

MR. WESSEL: Right. Judge Rosen if a colleague of yours called you from some random federal court say in Chicago (laughter) and says I've been asked to get involved in straightening out this mess, what are the one or two lessons that you learned in Detroit that you think I should keep in mind in Chicago?

JUDGE ROSEN: Say no. (laughter) My goodness. That was a great question.

SPEAKER: That's a first.

JUDGE ROSEN: Well fortunately--

SPEAKER: I know a lawyer if you need one. (laughter)

JUDGE ROSEN: Fortunately, in Detroit we didn't go over the cliff. (laughter)

Seriously, I would encourage them to get involved if they care about their city at all. You know I was a life time Detroiter and other than a few forays in Washington and Europe I lived in Detroit all my life so when Judge Rhodes asked me to do this, you know, all of that kind of flashed though my mind. It wasn't simply an assignment.

But I have to say one of the animating forces for all of us in the bankruptcy, I think Judge Rhodes, certainly the emergency manager, Kevin Ore, the governor who sort of put it all into motion, and me as the chief mediator was-- you know, never waste a good crisis. It wasn't enough, I think that will be true in any other municipality, it wasn't enough to simply get through this as best we could. Detroit was so far beaten down and it was something that had happened over six decades.

MR. WESSEL: Right. I'm trying to get you to tease out things that apply to Chicago or some other city (laughter). What lessons or-- Detroit was in many respect unique but in many respects it's not unique.

JUDGE ROSEN: Right. So let me-- the four lessons that we learned in Detroit and I say we, the mediators, but I think there was a broader lesson for everybody. What I would call the four C's. The first is candor.

You know what we found at the beginning of the bankruptcy was parties were in denial. They were in denial about the structure debt problems, they were in denial about the true level of service delivery and solvency, they were in denial across the board and as we begin talking about the creditors all the creditors, and to the city folks, you know we said denial is a river in Egypt, it's not a way to move forward.

MR. WATKINS: You should retire that joke. (laughter)

JUDGE ROSEN: It started with Mark Twain. And he's pretty good by me. I may find a Churchill quote in there somewhere too.

MR. WATKINS: I'll help you find a (inaudible)

JUDGE ROSEN: At any rate, the first thing was candor. Not just with each other, the parties with each other because a lot of time the parties are talking past each other, but with themselves. Looking themselves in the mirror and saying you know there really is tremendous structural debt and there is plenty of blame to go around here. We don't need to talk about portioning the blame on the same spectrum as a portioning of the division of the debt. That wasn't very productive. But you had to kind of go through that ventilation process at the beginning. So that's the first thing, candor.

The second thing is then to try and move to a stage of cooperation. And that was kind of my job as the mediator, to get the parties together and the earlier the better. A lot of what I've heard here this morning and this afternoon is-- I can't help to think that it could have been avoided with a good, I don't want to call it a mediation process because that sort of implies litigation but a good facilitation of discussion between the various creditor groups and the municipalities as early as possible. You know a good honest, candid, as the diplomats say full, frank, and candid discuss. So that's the second, Cooperation.

The third-- and you know everybody asks me if Detroit has a lesson for other municipalities and you know we had what was corporately called the "Grand Bargain" which I get credit for. I sort of came up with the idea but I didn't come up with the name but, creativity. I do think every municipality has a Grand Bargain somewhere. They may not have an art museum to leverage but there is a Grand Bargain somewhere. Everybody city has human assets, every city has physical assets, every city has revenue assets, so focus on creative ways to leverage those assets. And each one is going to be different for sure but smart people who can get on the same team and look down the road not just to get their piece of the pie but to make the municipality healthy so that there will be a bigger piece of the pie on the other end can be very creative.

You know the Grand Bargain was just one. We had many creative-- many creative things we did in the bankruptcy. The last two deals we did with Senquora and Figics the insurers of the COPS debt were very creative. We ended up partnering the city with the-- those two creditors which you know, they were pretty vigilantly defending their positions. But we partnered them together so that in the future they are going forward together and they may end up coming out very, very well because real estate value in Detroit, we gave them, we gave Senquora a 20 year extension on the lease, on the tunnel to Chicago and a bunch of properties right around which as the real estate values are now rising in Detroit those are really going to rise and Fidget who are the insurer of about 1.1 billion on the COPS debt, we gave the property on the river to underneath Joe Lewis which is moving to midtown, we gave that to them and they're talking about opening up the river to what we call the west river to the bridge and putting up a 30 story hotel in Congo and opening it all up for retail and so on paper they only got 13.7 cents on the dollar down the road that can be very, very-- so that was another aspect of creativity. And each little deal had its own creative element to it.

Finally, and I can't stress this enough, courage. That-- as I reflect on Detroit, Detroit is really not a series of deals over 16 months many of which were concluded over pizza at 2:30 in the morning. It's really about people. It's about people from all different walks of life, backgrounds, strata, coming together to put behind them the mistakes and ghosts of the past to come together and take a leap of faith to find out what really is the best interest-- I mean in Detroit we could have had (inaudible) litigation for a decade with the many cert-worthy, cert-worthy for those who aren't lawyers issues who could have gone up to the Supreme Court. But there would have been nothing left of Detroit but dust and who would have profited from that. So-- I think if cities get ahead of the game earlier and begin a facilitation process they can come to agreements.

MR. WESSEL: Interesting.

MR. WATKINS: Rolling back to your question for a minute on low rate and what impact does that have. So from where I sit what it means is less discipline by the investor community so we're-- I mean there are no surprises. We had a great session that Louis did on the whole OPEB thing. There are no surprises on where the fiscal mismanagement lies in this country. And I have to say that it's not systemic issue, that these are out-liars and tails if you will and not representative of the muni-space in general so I don't think there is any systemic risk out there but you know it happened in Detroit, it happened in Puerto Rico, those are common elements is the continual wiliness to the investor community to step up and provide credit and with spread compression and the search for yield that discipline-- what little discipline if there is any abates because for a very, very small-- for a few basis point they're willing to take on extraordinary risk relative for the return that they're getting and that's what the low interest rate--

JUDGE ROSEN: Don't forget about the fees for the insurers as well as lubricating some of these deals. If you look at some of the fee structures in Detroit for the insurers, all of the premium is paid up front you can understand why they took the extraordinary risks that they took.

MR. WESSEL: Natalie, you asked the question of the governor of Puerto Rico, I'm not sure that he-- if he had a crystal ball he had his sunglasses on or something, right. Is this the beginning of the end of the Puerto Rico crisis or is this just chapter-- or the second inning in a nine inning game?

MS. COHEN: It's an open question. They haven't appointed the members of the board yet. That's a very critical aspect of how this moves forward and I had also talked about buy-in as far as who the next governor might be, the local-- you know, the guy on the street, the administrator that has the ability to somehow undercut some of the efforts that may get put forward.

Detroit as well, getting the street lights back into place, the bankruptcy process is a tool and it is just a baby step in the beginning. So you know, unfortunately with the case of Puerto Rico Congress is the overseer so to speak and right now in this period of time there are conventions coming up and there are a lot less attention to next steps and will they actually-- will Congress, will they come back and look at the legislation that gets proposed by the economic task force. This is what you could do to revive-- I was delighted to hear the governor say they have to maintain the University of Puerto Rico.

Again, to Judge Rosen's point you have to as a community look at what you're assets are and do an inventory. What are your assets and every community does have some sort of an asset whether it's people or it's local or it's the infrastructure and so on and then build on that and that's something that they clearly can do in Puerto Rico.

MR. WESSEL: What about the ripple effects in Puerto Rico. I've heard two versions of this. One version is it's a territory, it's a rather unique situation, yeah it might apply to Guam but after that it's not going to make much difference. But other people say, not so quick, that there are elements of this legislation that, this has become socially acceptable and we may find that things have been put in to PROMESA whether it's some things like the minimum wage or the way the oversight board is structured or its power.

MS. COHEN: I think-- and this came out in the conversation, any time there is an oversight body and this was definitely true in Detroit, it's clearly been true in a lot of other examples. D.C. was another example. There is an outcry that this is an abusive democracy. I reverence DuBos I actually saw him on television say I'd rather burn down the city of Detroit than have the State come in. You get into race relations you get into colonization, that's what we're talking about here. The issue of status in democracy inevitably has come into play. And so-- I feel and say in North Carolina you have the government commission, I've talked with many public officials at the local level, they say well we never could have done anything that Detroit does because we have this oversight. They're not crying that democracy is being abused or stepped on or whatever, it's just their way of doing business. That's the relationship they have with the state and they accept it.

So, I hope that-- and I think in Detroit people have gotten past that perspective, I don't know, I'm not on the ground there and I hope that in Puerto Rico that kind of-- I think it's actually more intense in Puerto Rico because the parties are defined by status. You have the Statehood party, you have the Independence party, and then you have the Commonwealth party. Anyone growing up there are aware of that status, of that inferiority of services that come from the federal government. That is part and parcel of their identity even more so than in Detroit and--

SPEAKER: So then Ben, does Puerto Rico make a difference to the state of Florida, how this is resolved there?

MR. WATKINS: Other than being the beneficiary (inaudible) but we prefer rich people from New York, New Jersey, and Illinois (laughter) naturally falling into our state -- (laughter)

SPEAKER: We're working on that. (laughter)

MR. WATKINS: -- that's the growth industry. But we -- it does matter and I do think it has presidential value and it clearly is a mixed bag. So while I appreciate the governor's arguments about the impairment of independence the over-side board, at least from our perspective, is a critical element that I think can work. And-- because they demonstrated their inability to properly manage their own affairs is the only reason the oversight board is their, so it's sort of a condition president and in many cases takes the heat off of the elected officials for someone to come in from outside and take responsibilities and be the bad guy, so it can be helpful.

The other part of that that Natalie alluded to, the complexion of the board can affect the outcome dramatically and what I mean by that is I assume they would be fiscal conservatives, right. That's not necessarily the case. And if all they do is go in and facilitate and grab other issues that deal more fundamentally with funding and financial assistance then that's sort of a-- problematic from my perspective because that's more of a political issue but I guess most importantly the thing that most troubling-- so institutionally the issuer community is behind an orderly process for resolving the issues but we don't want a lot of other political issues--

MR. WESSEL: Thrown into that pot, yeah.

MR. WATKINS: -- thrown in to that pot but let's be straight and let's be technical and let's put the frame work in place. But the thing that is troubling to me most that could be presidential is that we have federal legislation that steps in and changes an order of priority under the constitution about how monies are dedicated and that's one thing that you need to-- our system of government and the way this market operates is the rule of law and certainty because you're loaning somebody money for 30 years and you think you know what you get in return for that and when courts come in or federal legislation comes in to trump that, which is in effect what has happened than that's troubling to me because I'm a states' rights kind of guy, I don't see a lot of good solutions emanating from your hometown, with all due respect.

JUDGE ROSEN: I won't put on you all the sins of Florida if you don't put on me all the sins of-- (laughter)

MR. WESSEL: Truce. George do you want to weight in. Wait for a mic.

MR. FRIEDLANDER: One observation from your earlier question about interest rates and than one about this-- that's really more of a question, about the Detroit and all.

In terms of interest rates the tragedy, and it was alluded to, is that here we have historically low interest rates and new money financing in the Newne market over the last five years is on a real-- (inaudible) basis is half annually of what it was in the 10 years before that. I think some of that relates to pensions, some of it relates to a remarkable state level move toward fiscal conservatism in some cases for some very wrong reasons but it is a tragedy that we have this remarkably low borrowing environment and nothing is being done about infrastructure.

Now back to the question of what could have been done in places like Detroit and Puerto Rico. My perception and Natalie in particularly, you're response on this, the distinction between a permanent oversight board allah North Carolina and what has happened in Michigan is an extraordinarily important one, the emergency manager structure in Michigan is extraordinarily unpopular and is perceived as being racial.

The fact remains, had their been some sort of oversight, structural oversight created by the state vastly earlier the way there is in North Carolina we never would have had Detroit. If it has been in place 15 years earlier the litany of incompetence and waste and self- dealings and fraud and so on that went on within Detroit and essentially destroyed it along with the problems of the auto industry probably would not have happened or at least not have been nearly as bad. There just isn't a structure in a lot of states to do things that are not all the way in the direction of emergency manager which is not-- which in most cases are not what's needed.

MS. COHEN: Well, thank you for that. I think if-- this came out earlier in terms of that discussion of oversight, some of the oversight programs are pre-default like in North Carolina and New Jersey and so on where it's just part of the operating business model. That's how you do things, the state looks at the budget, it is involved and has the power and engagement with the local government and knows where the problems are. And again, to the other points earlier, it's not just a monitoring process but it's a proactive engagement with the local government so I would say obviously that's preferable in terms of highlighting working with troubled governments where you come up with an ultimate great solution for the economy I don't know.

But Michigan-- the positive there, and I've done a little bit of writing about this, is that in addition to the Chapter 9 the state model actually has steps. It has a process. It has the appointment of a single quarterback that actually-- you know, the judge can talk with. Where as in a San Bernardino you have a change over in the council or the mayor or whatever and there's not necessarily a there,

there to work with or negotiate with. If you have a changing administration there isn't the quarterback in place like you have in Michigan. So I think it's on a spectrum actually. But obviously pre-default is a heck of a lot better than waiting until you get to the emergency level.

MR. WATKINS: To add to that, I think--

MR. WESSEL: Go ahead, I just want to get the mic to Bill over here--

MR. WATKINS: There is a trend in the legislation to have more oversight, more monitoring. There are a number of recent legislations in Nevada and Indiana and so forth so I think we're going to see a trend in trying to address this. I think another issue that is important in the oversight is to make sure we don't sort of misunderstand what the mission is and by that I mean the principals of municipal finance and government finance is extremely important as far as predictability. The more the state can set those priorities up the better off you are.

Why do I say that? The spread even now between a good rate bond a not very good rated bond could be 200 basis points. What's 200 basis points, I'm going to do simply math okay, 200 basis points over 30 years is 60 percent of the principle that you're paying-- that you're not using for infrastructure and providence. That you're not using to pay pensions or improve services. So I think it is so important-- and that's why I think our legislatures are pretty much laser focused on, how do I reduce the borrowing cost. If you walk over the principles of Edmond Finance the only thing I can assure you of, just like Argentina and Greece has experienced it and others, all you're going to see is that yield on the bond go up.

MR. GLASCAL: Yeah, I'm Bill Glascal. I agree with the comment that-- the question that George made about new money-- there is a tremendous reluctance on whether it's on pensions in some cases or whether it's crowding out new money or whether it's debt is a bad word and the revenue is not there or nobody wants to raise taxes, it is what it is.

I looked just a few minutes ago, the yield on AAA 10 year bond on the Blueberg is 1.37 percent this afternoon.

SPEAKER: Treasury.

MR. GLASCAL: No. The AAA munities is 1.37 percent. So why hasn't-- why hasn't Puerto Rico, 70 billion dollar default, Puerto Rico, Detroit, Illinois, New Jersey, Harrisburg, sort of a-- the

California bankruptcies, why hasn't this really unsettled the market or what should we be looking for-- what should we be looking for? What's going to happen down the road? Will this have a longer term effect even if right now it's not showing up in yield?

MS. COHEN: Well, I'm hopeful that after November things might settle down and I definitely see that in the last couple of weeks there has been more borrowing, that the states have come in-- I mean, I think there is a confusion between Washington and at the state-level that states typically borrow for infrastructure. They are borrowing for capital improvements. They're not for the most part borrowing to fill deficits and I think that there is kind of that confusion on the Hill around that concept, the states borrowing too much.

And some of that has affected some of the governors in their thinking but it is a pre-election year. There is a very strong anti-tax, anti- any kind of change in the financial structure. It's very unfortunate because we do see, I have charts, I'm happy to send them out to people, after 2010 the new money infrastructure borrowing dropped precipitously and you can pull a million economic studies that say if you have a good transportation system, a good airport, a good water system, all of those things are non-partisan. You know turning on the tap and getting good clean water out should not be a partisan issue in my opinion.

MR. WATKINS: So I can give you anecdotally and I can have a data set of one extrapolate to an entire population, I have no problem with that at all. (laughter)

SPEAKER: I think you could get a good career in journalism with that. (laughter)

MR. WATKINS: So it's political sentiment, part of it is political sentiment and part of it is economic. The political sentiment is my boss is a tea party guy. He's an anti-debt kind of guy. The second part of that is--

MS. COHEN: He drinks water. And he wants to have clean water.

MR. WATKINS: Yeah, we've got all that already so that's a non-issue. Come to Florida, it's a great place to live. We don't have those kind of troubles.

MR. WESSEL: You have global warming. A global warming problem.

MR. WATKINS: Well, that's solvable.

So there's a-- the other is an economic issue which is hangover from the great recession. We're cutting funding for healthcare, education and borrowing more money at that time there's a political-- you're saying you're cutting, cutting, cutting, cutting and so you have that pervading the consciousness of the people making that decision.

So those are the, in my judgment, the reason why. So from an economic and an academic standpoint it's absolutely the right thing to do but from a very practical, political level there are head wounds involved.

MR. WESSEL: And so, I was going to-- sure. Last word.

SPEAKER: Last question. I get the last word. (laughter)

You know one idea you talk about this-- it's kind of interesting we've all been talking about why don't we take advantage of the debt being so low, the rates. But on the other hand you look at the balance sheets and I know there are critics of the Gasby's new reporting but I think there is a lot of truth in the Gasby new reporting. You look at the balance sheet for many cities, states, counties, debt is actually going up right now because of the pension situation. And you know what, so I think you would say-- in fact it could even go more, with Chicago now with its pension funds, the new discount rate is 4 percent for those funds and probably going in the other direction for the other two, so it's even going to go up more. But you know it brings up the idea which I know how unpopular this is and so am I, I'm against it at the moment but I think maybe there is a way to work it out, we have to keep an open mind for it. This may be the time to consider some pension bonds which at these rates--

SPEAKER: Oh my gosh. (laughter)

SPEAKER: Let me finish this--

JUDGE ROSEN: We tried that in Detroit in 2005, 2006. That didn't work out very well.

SPEAKER: Actually I had you in mind when I mentioned that. But not only in Detroit were they in bankruptcy taken out, they were in California obviously too and even in Illinois where we did the 10 billion dollar deal in 2003. These were all misadventure that were done either with bad securities, weak securities. They weren't GEO or limited tax. Well, in California they weren't. We'll find out how good GEO's are at Illinois, we're going to find that out eventually but in Calif-- in Illinois case the fact is that they did it with the idea that they were putting a reform plan in place that never happened.

So I would only say I would support this if it would be really truly tied to an iron clad reform really that's obvious to everyone. But I bring it out, I bring out very unpopular ideas because I think we need to think about these kind of things if borrowed debt is at 2 percent for the better issuers on the long term and not on the COP like we did in California and Detroit but if we did these things at two to four percent because taxable borrow markets made it very easy, we might actually have something we could actually do but only if it's in with an iron clad reform plan.

So I offer a very unpopular idea, I wanted to go home very unpopular-- (laughter)

MR. WATKINS: Yes, thank you. So this has been a very long day and I'm impressed with the attention span with the people in this space. I want to thank Rich and Dan who brought this to us, my colleague Louise, Carrie, Peter, Lillia, and Anna who helped us with logistics. I really did mean what I said this morning, that this is a bit of an experiment for us. We'll reflect on it whether we want to do this again with you guys (laughter), it's been very interesting. We've learned a lot. I want to leave by asking you to help us make this better in the future. So you will get some form some survey money or something or you can just email me at DWessel@Brookings.edu. We're interested in what you found useful here and what not and also what themes, unanswered questions you have because we have the luxury if we start soon of maybe getting some good work, scholarly work done on questions as opposed to taking advantage to stuff that already beginning to blossom on the tree. So with that I'm going to call it a day and close and thank all of you for your attention. (applause)

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