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Down the Wells

Wells Fargo's Payday Loans Have Left Puerto Rico Billions of Dollars in the Hole

Puerto Rico is embroiled in a dire humanitarian crisis that is being compounded by its unsustainable debt load. Congress passed the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) in June 2016, which created a Fiscal Control Board to oversee the Commonwealth's finances. But in order for it to do its job fairly, the Control Board must understand how Puerto Rico came to be so deeply indebted in the first place. The ReFund America Project is releasing a series of reports investigating Puerto Rico's debt. Our previous reports can be found on our website, at refundproject.org/#puerto-rico.

Wells Fargo played a critical role in pushing Puerto Rico to take on unsustainable levels of debt, contributing to the financial crisis that engulfs the island today. Wells Fargo and Wachovia (which Wells Fargo acquired in 2008) targeted the Commonwealth with predatory payday loans that have left Puerto Rico billions of dollars in the hole.

...an effective interest rate of 734 percent!

Wells Fargo and Wachovia were one of the underwriters on seven different issuances of capital appreciation bonds to Puerto Rico. A capital appreciation bond (CAB) is a long-term bond with compounding interest on which the borrower does not make any principal or interest payments for the first several years, and, in some cases, until the final maturity of the bond. As a result, the outstanding principal actually grows over time because the unpaid interest gets tacked on to the amount owed, and then the borrower has to pay interest on the interest. Because of this structure, borrowers often end up paying extraordinarily high interest rates over the life of the bonds. In this way, a CAB is like the municipal version of a payday loan.

Capital Appreciation Bonds that Wells Fargo & Wachovia Helped Underwrite

Bond	Initial Principal	Total Interest	Effective Interest Rate
2011A COFINA Bonds	$380 million	$3.5 billion	913%
2011C COFINA Bonds	$102 million	$434 million	427%
2010A COFINA Bonds	$130 million	$535 million	412%
2010C COFINA Bonds	$98 million	$517 million	529%
2009B COFINA Bonds	$54 million	$291 million	543%
2007A COFINA Bonds	$1.7 billion	$13.2 billion	793%
2007B COFINA Bonds	$147 million	$450 million	306%
Total	**$2.6 billion**	**$18.9 billion**	**734%**

Wells Fargo and Wachovia helped underwrite seven issuances of these payday loans to Puerto Rico, which have an outstanding balance of $21.5 billion. However the underlying principal on these bonds is just $2.6 billion. The remaining $18.9 billion is interest—an effective interest rate of 734%!

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Each of these CABs is legally dubious because it was issued by the Puerto Rico Sales Tax Financing Corporation, known popularly by its Spanish acronym, COFINA. The COFINA structure was created to refinance what was considered at the time to be “extra-constitutional” debt—a term that no one has ever defined but which calls its legality into question.

This is illegitimate debt that Wells Fargo and other banks sold to Puerto Rico. In fact, most of it is not even debt. 88% of it is interest! **Puerto Ricans should not be forced to pay for these payday loans. Furthermore, Wells Fargo should pay back the fees it charged Puerto Rico for these predatory deals.**

A Note About Our Numbers

We used bond-level data from Bloomberg to analyze Puerto Rico’s debt in this document. However, there are significant inconsistences in the data from Bloomberg and the official debt numbers being put forth by the Puerto Rican government. For example, in November 2015, the Commonwealth reported only $15.2 billion in total COFINA debt in its Financial Information and Operating Data Report. However, according to the Bloomberg data, the Commonwealth has $36.9 billion in COFINA bonds—more than double the official number. We strongly urge a complete audit of the Commonwealth’s debt to ensure complete transparency and accountability.

About the Authors

Saqib Bhatti and **Carrie Sloan** are with the **ReFund America Project** (RAP) of the **Action Center on Race & the Economy** (ACRE). RAP tackles the structural problems in the municipal finance system that cost governments across the United States billions of dollars each year at the expense of public services. ACRE also helps lead the **Forgo Wells** Coalition, which seeks to hold Wells Fargo accountable for its predatory and racist business practices that harm communities around the globe. Bhatti and Sloan research the role of financial deals in contributing to public budget distress and work with policy experts, community leaders, and public officials to develop, advocate for, and implement solutions to save taxpayer dollars.