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Puerto Rico Power Utility Says Debt Exchange Plan Unworkable.

The Puerto Rico Electric Power Authority said a bondholder proposal to restructure the utility's debt isn't achievable because it imposes disproportionate risks on ratepayers and other creditors.

A group representing owners of 40 percent of the securities unveiled a $8.1 billion debt exchange Thursday that would delay payments for several years and give the junk-rated agency $2.5 billion to upgrade power systems. The utility, known as Prepa, has been negotiating with creditors including mutual-fund provider OppenheimerFunds Inc. and hedge fund BlueMountain Capital Management LLC for almost a year on how to overhaul its finances.

The plan "does not provide a path for a successful restructuring," Yohari Molina, a spokeswoman for Prepa in San Juan, said in a statement. "It does not share the burden."

Under the plan, debt-service payments would be suspended on existing securities and interest payments reduced by selling new obligations that would be repaid from a surcharge on Prepa's customers. Delaying principal payments would free up about $2.5 billion through 2025 to upgrade plants and diversify fuel sources for commonwealth's main electricity provider. A June 1 proposal from Prepa included at least $2.3 billion to rehabilitate facilities on the island, where electricity costs are double those on the U.S. mainland.

LIPA Example

"It almost creates interest-free borrowing for the island's utility," Tom Wagner, co-founding partner of hedge fund Knighthead Capital Management, said Thursday during a Bloomberg television interview. Knighthead owns Prepa bonds.

New York's Long Island Power Authority used a similar financing, Wagner said. Bondholders plan to continue their "constructive" talks with Prepa on the plan, he said.

Assured Guaranty Ltd. also has concerns about the bondholder's latest plan, although borrowing off of a new fee would help improve the utility, Ashweeta Durani, a spokeswoman for the Bermuda-based bond insurer said in an e-mailed statement.

"While we do not support the recovery plan proposal released last evening by the ad hoc bondholder group, we believe that a properly structured securitization transaction could play an important role in Prepa's recovery plan," Durani said.

While such a financing could be the foundation of a long-term plan, "the proposal was developed without consultation with bond insurers and disproportionately impacts our interest," Kevin Brown, a spokesman at MBIA Inc.'s National Public Finance Guarantee Corp., based in Purchase, New York, said in an e-mail.

The two bond insurers guarantee about $2.4 billion of Prepa debt.

Default Speculation

Puerto Rico and its agencies amassed $72 billion of debt by borrowing to fill budget gaps as the island's economy has struggled to grow since 2006. Governor Alejandro Garcia Padilla last month said the commonwealth can't afford to pay its debts, igniting concern it will default. Officials are set to draw up a restructuring proposal by Sept. 1.

The utility in August 2014 signed a contract with investors, banks and bond insurers that keeps negotiations out of court, called a forbearance agreement. Prepa must craft a debt-restructuring plan by Sept. 1 or that accord will expire. The utility avoided defaulting on a July 1 bond payment with the help of a loan from bond insurers.

Forbearance Pact

OppenheimerFunds, the biggest holder of Puerto Rico debt among municipal mutual-fund providers, Franklin Templeton Investments, Angelo Gordon & Co., Knighthead Capital, BlueMountain Capital and units of Goldman Sachs Group Inc. have signed the forbearance pact.

The creditor's proposal would delay principal payments for an average of 7.8 years and cut the coupons on as much as $5.7 billion to an average rate of 4.1 percent from 5.24 percent. Another $2.4 billion of securities would be sold as capital-appreciation bonds, which would push out principal and interest costs for up to 19 years.

The first tranche of current-interest bonds would be issued at a price of about 150 basis points above benchmark tax-exempt debt and the capital-appreciation bonds would be priced at about 200 basis points above top-rated munis, according to the bondholder plan.

Prepa's customers would be charged a new fee, with that revenue stream repaying the bonds. Under the plan, Prepa clients would pay an average 24 cents per kilowatt hour compared with the utility's historical rate of 28 cents. That surcharge may prove to be a tough sell.

"It's very hard to see how the politicians can line up behind this proposal," said Daniel Hanson, an analyst at Height Securities, a Washington-based broker dealer, said in a telephone interview.

Prepa bonds maturing July 2042 traded Thursday at an average price of 56.2 cents on the dollar, the highest since June 8 and up from 49 cents Wednesday, data compiled by Bloomberg show. The average yield was 9.6 percent.

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