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Puerto Rico Utility Reaches Deal With Bond Insurers in Effort to Avoid Default.

Puerto Rico's beleaguered electric utility announced new progress late Wednesday in its continuing efforts to avoid a default on as much as one-eighth of the island's total debt of $72 billion.

Officials said that two bond insurers had agreed to take part in a five-year restructuring plan for the Puerto Rico Electric Power Authority, an islandwide monopoly. The insurers' involvement signaled that Prepa had found a way to satisfy its bondholders, who expect to be paid about $177 million on Jan. 1, without having to part with that much cash itself.

Prepa is one of 13 branches of the Puerto Rican government scheduled to make bond payments on Jan. 1, for a total of around $902 million.

Cash is in short supply, and the island's governor, Alejandro García Padilla, has warned that if he must choose between paying bondholders and providing essential public services, he will provide the services. His warnings have given rise to intense speculation as to which types of bond debt may be paid, and which may not.

The bond insurers participating in the restructuring deal were said to be operating units of Assured Guaranty and National Public Finance Guarantee. An official with knowledge of the negotiations said a third bond insurer with a smaller exposure, Syncora Guarantee, might join the process later.

On Jan. 1, the two participating bond insurers will purchase $50 million of new revenue bonds from Prepa; a creditors' committee known as the Ad Hoc Group will purchase an additional $65 million worth of bonds. Those purchases will give Prepa $115 million of fresh cash, which it can use to honor a large part of its scheduled bond payment due that day. Prepa is expected to make the rest of the payment out of its own resources, according to people familiar with the talks.

In other respects, the restructuring plan resembles terms that were made public earlier this year. They called for giving Prepa five years' worth of interest-rate relief, which would save the utility more than $700 million.

In addition, the creditors have agreed to permanently reduce Prepa's outstanding bond principal by more than $600 million, according to a summary provided by the utility. This would be accomplished through a debt exchange, in which the holders of Prepa's current, junk-rated bonds could turn them in and receive new investment-grade bonds.

Lisa J. Donahue, Prepa's chief restructuring officer, said that to make sure the new bonds qualify for investment-grade ratings, the two bond insurers had agreed to backstop them by posting a type of financial guarantee, called a surety. The idea is to make investors want to exchange their shaky old bonds for the new ones, despite the lower face value, by making the new bonds a better credit risk.

The debt exchange is not expected to take place until next summer, and, until then, the negotiators must steer the deal around a number of obstacles. The first will fall no later than Jan. 23 — a deadline for the Puerto Rican legislature to pass enabling legislation for the deal. Legislators have so far shown little appetite, because they would also have to request a rate increase for Prepa.

Elected officials anywhere would be reluctant to authorize a rate increase in an election year, but in Puerto Rico the increase would come in the wake of new taxes imposed because of the financial crisis, school and hospital closings, and other painful austerity measures.

In addition, a large number of Prepa's bondholders continue to stay aloof from the restructuring talks, perhaps hoping an even better deal might appear later.

The creditors on board so far represent about 70 percent of Prepa's $9 billion debt; they include the Puerto Rico Government Development Bank, mutual funds, hedge funds, and banks that finance Prepa's fuel purchases.

The holders of the remaining 30 percent of the debt have not yet signed onto the deal, and it is not clear whether enough of them ever will, at least under the incentives proposed by the current deal. But one more factor is expected to come into play in the first half of 2016: There are signs that Congress is preparing to make some form of bankruptcy protection available to Puerto Rico.

Currently, none of the island's government bodies have any legal standing to take shelter in Chapter 9 municipal bankruptcy. But that could change soon, and the bankruptcy laws include what are known as cramdown provisions, which make it possible for a bankruptcy judge to force holdout creditors to accept a deal.

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