S&P Global
Ratings

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Summary:

Long Island Power Authority, New York; Retail Electric

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Summary:

Long Island Power Authority, New York; Retail Electric

Credit Profile		
US$407.74 mil elec sys gen rev bnds ser 2016B due 09/01/2046		
Long Term Rating	A-/Stable	New
Long Island Pwr Auth elec (AGC)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec sys gen rev		
Long Term Rating	A-/Stable	Affirmed

Rationale

S&P Global Ratings has assigned its 'A-' rating to the Long Island Power Authority (LIPA), N.Y.'s (LIPA) $407.7 million electric system general revenue bonds, series 2016B. At the same time, S&P Global Ratings affirmed its 'A-' rating on the utility's parity senior-lien revenue bonds. The outlook is stable.

More than 80% of the bonds' proceeds will fund portions of LIPA's capital program. The bonds will also refund some of the utility's existing debt.

Uniondale, New York-based LIPA pays its unsecuritized bonds' debt service from the net revenues of its retail electric system operations. As of Sept. 29, 2016, the utility reported $3.0 billion of unsecuritized long-term debt, and $500 million of short-term debt. Long-term unsecuritized debt is nearly $800 million lower than it was as of Dec. 31, 2015, largely because of two 2016 securitization transactions that refunded portions of LIPA's unsecuritized debt. The utility also records on its balance sheet $2.4 billion of capital lease obligations that reflect the net present value of its commitments to make fixed payments to its power suppliers.

Although LIPA's financial statements consolidate it unsecuritized debt and the debt of the Utility Debt Securitization Authority (UDSA), the vehicle for issuing LIPA-related securitization bonds, those bonds' debt service is subject to a separate pledge, are not an obligation of the authority, and do not have a claim on the revenues pledged to the utility's unsecuritized debt. LIPA acts as the servicing agent for the UDSA debt and uses its retail bills to collect UDSA debt service from its customers. It remits the separately pledged revenues to UDSA.

In 2016, UDSA sold $1.1 billion of securitization bonds in two series. The 2016 bonds were in addition to the $3 billion of securitization bonds sold in 2013-2015. It can issue up to $4.5 billion of bonds to retire portions of LIPA's debt and $370 million of securitization bonding capacity remains.

We calculate financial ratios net of UDSA debt and debt service. Our fixed charge coverage treats capacity payments to other generation suppliers as debt service in lieu of an operating expense because we view those payments as funding the suppliers' recovery of their capital investments in the generation they dedicate to LIPA. We calculate fixed charge coverage by removing consolidated UDSA revenues from the income statement, taking out UDSA debt service from total debt service and treating the capacity charges paid to National Grid and other suppliers as debt service by adding that amount to the numerator and denominator of the debt service coverage ratio calculation.

The rating on LIPA's unsecuritized debt reflect our opinion of the following favorable credit factors:

- Securitization transactions have reduced unsecuritized debt balances by more than 50%. These reductions could improve the financial cushion available to the unsecuritized bondholders. However, LIPA's high capacity payment commitments to power suppliers will dilute some of the remaining unsecuritized debt's debt service coverage ratio improvements because our analysis focuses on fixed charge coverage and the ratio of capacity charges to unsecuritized debt service is increasing as the utility reduces its unsecuritized debt balances.
- LIPA benefits from the stable revenue stream that its approximately 1.1 million customers provide.
- The utility derives 53% of its revenues from residential customers and the balance from commercial and governmental customers. LIPA principally serves customers in New York's Nassau and Suffolk counties, where income levels in 2015 were 160% and 150% of the national household effective buying income, respectively, which we consider very strong.
- In 2015, New York State's Department of Public Service recommended and the LIPA board adopted multiyear base rate adjustments. This increased revenues by $20.1 million in 2016. Subsequently, the utility will add to base rates an additional $65 million beginning in 2017 and $64 million beginning in 2018.
- Beyond base rates, retail rates include monthly and other periodic adjustment mechanisms for recovering changes in sales, purchased power costs, delivery costs, debt service, storm costs payments in lieu of taxes, and other adjustments. We consider the presence of these mechanisms as supporting revenue stream stability. Significant among the adjustment mechanisms is a revenue decoupling mechanism that provides for the collection of revenues deemed to have been lost to energy efficiency programs, distributed generation, weather and changes in economic conditions. The revenue decoupling mechanism trues up twice a year and LIPA is exploring moving to an annual adjustment, which we view as providing less protection to cash flows than more frequent adjustments.
- We view retail rates as competitive for the region, although they are high in absolute terms.

The rating also reflects our view of these credit risks:

- LIPA faces substantial fixed costs in connection with its power supply arrangements and these costs constrain the utility's fixed charge coverage. Although the securitizations and approved rate adjustments could improve coverage as more utility debt migrates to UDSA in 2016 and retail base rates increase in 2016-2020, fixed charge coverage remained adequate in 2015 at 1.1x, following 1.2x in both 2013 and 2014. The ratio of fixed charges to debt service might rise following the securitizations, which could constrain fixed charge coverage.
- Customer bills include securitization debt service charges, and LIPA previously projected that converting portions of its debt portfolio to securitized will not reduce customer bills, which we view as having the potential to frustrate the utility's ability to placate customers and politicians that have expressed displeasure with rates.
- Legislation provides for regulatory oversight of ratemaking if requests for rate increases exceed prescribed thresholds, which might diminish LIPA's ratemaking autonomy and the rate oversight distinguishes the utility from most other public power utilities.

The authority is among the three largest public power utilities in the U.S. by customers and revenues. It serves about

1.1 million retail customers. Unlike similar-size peers, LIPA primarily relies on others to supply its customers' electricity needs, purchasing all but a small portion of its electricity from third parties. LIPA's owned generation capacity consists of a 224-megawatt (MW), 18% interest in the Nine Mile Point 2 (NM2) nuclear plant, which equaled about 4% of 2015's 5,049 MW peak demand. The nuclear plant is co-owned with and operated by Constellation Energy Nuclear Group LLC. Contractual agreements with National Grid USA and other energy providers, as well as market purchases, serve all needs beyond NM2. The power supply agreement with National Grid expires in April 2028. It allows LIPA to purchase energy from resources other than National Grid's if they have lower costs, which is important because National Grid's resources have high production costs. National Grid provided nearly 25% of LIPA's 2015 power supply. The cost of reserving this capacity does not abate when LIPA purchases power from others. Two underwater transmission cables provide access to the PJM and New England independent system operator markets, which helps reduce LIPA's exposure to National Grid's high production costs.

Widespread dissatisfaction with high rates and inferior service historically contributed to politicization of rate-setting. The authority's poor response in the wake of Superstorm Sandy culminated in the passage of the LIPA Reform Act, a three-year rate freeze, and the utility's diminished rate-setting autonomy. The New York Department of Public Service must review rate proposals that seek to increase revenues by more than 2.5% per year. In our view, the rate-setting construct could reduce financial flexibility. The Reform Act also transferred much of the day-to-day operating responsibilities to PSEG-Long Island (PSEG-LI), a subsidiary of New Jersey's Public Service Enterprise Group (PSEG), an investor-owned, diversified energy company. Under an operating agreement that expires in 2025, LIPA pays PSEG-LI an annual fee that contains performance-based incentives. The authority's contractual obligations to PSEG-LI include substantial unfunded pension liabilities and post-employment benefits relating to the PSEG employees that serve the LIPA territory.

The Reform Act directed the utility to file a 2015 rate application with the New York State Department of Public Service (DPS), which conducts evidentiary hearings. On Sept. 28, 2015, DPS issued its rate recommendation to the LIPA board, which ratified it. The DPS based its recommendation on debt service coverage analysis in lieu of targeting returns on assets or equity as is common to investor owned utilities. As is the case with other regulated utilities, LIPA has not received guarantees that it will achieve specific coverage metrics, but the several adjustment mechanisms the DPS established for addressing changes in prescribed variable costs, should promote sound credit quality. Significant among the adjustment mechanisms is a revenue decoupling mechanism that provides for the collection of revenues deemed to have been lost to energy efficiency programs, distributed generation, weather and changes in economic conditions. The revenue decoupling mechanism trues up twice a year and LIPA is exploring moving to an annual adjustment, which we view as providing less protection to cash flows than more frequent adjustments.

S&P Global Ratings generally excludes nonrecurring grant income from its debt service coverage ratio calculation's numerator. However, part of the grant income that LIPA reported on its income statement in recent years principally represented Federal Emergency Management Agency reimbursements for storm damage repairs that the authority expensed, and U.S. Treasury reimbursements for a portion of gross interest on Build America Bonds. Therefore, we included the grants in the coverage ratio's numerator. We also added the income statement's recovery of carrying charges on regulatory assets to the numerator. This money represents collections of debt service on bonds issued to finance a bill credit that coincided with the authority's inception.

The utility recorded more than $600 million of unrestricted cash and investments on its balance sheet as of Dec. 31, 2015, which we view as representing a sound two months' of operating expenses. More than $208 million of cash restricted for working capital requirements brings this ratio up to about three months' operating expenses.

Outlook

The stable outlook reflects the 2015 rate decision, which removes some of the uncertainty that overshadowed the first time application of DPS rate oversightto a New York public power utility. The outlook also reflects the availability of adjustment mechanisms that can limit the effects of volatile variable revenues and costs and our expectation that the interplay of rate increases and additional securitization financings could stabilize and possibly strengthen fixed charge coverage.

Upside scenario

We could raise the rating if fixed charge coverage materially strengthens because of rate increases and the use of securitizations.

Downside scenario

We could lower the ratings if capital spending needs materially add to unsecuritized debt or resistance to rate increases pressure fixed charge coverage ratios.

Ratings Detail (As Of September 30, 2016)		
Long Island Pwr Auth elec sys		
Long Term Rating	A-/Stable	Affirmed
Long Island Pwr Auth elec sys gen rev bnds ser 2016A due 05/01/2033		
Long Term Rating	A-/Stable	Affirmed
Long Island Pwr Auth elec sys gen (AGM)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec sys (AGM)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec sys (MBIA) (ASSURED GTY)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (wrap of insured) (FGIC & AGM) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (wrap of insured) (FGIC & ASSURED GTY) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (wrap of insured) (FGIC & BHAC) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (wrap of insured) (MBIA/National) (AGM) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (wrap of insured) (SYNCORA GTY) (ASSURED GTY) (BHAC) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed

Ratings Detail (As Of September 30, 2016) (cont.)		
Long Island Pwr Auth elec (wrap of insured) (SYNCORA GTY) (ASSURED GTY) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (wrap of insured) (SYNCORA) (MBIA) (National) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (AGM)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (AGM)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (ASSURED GTY)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (BHAC)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (BHAC) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (BHAC) (SEC MKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec (CIFG)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth retail elec (BAM)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth retail elec (BAM) (SECMKT)		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Long Island Pwr Auth elec		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
New York St Energy Research & Dev Auth, New York		
Long Island Pwr Auth, New York		
New York St Energy Research & Dev Auth (Long Island Pwr Auth)		
Long Term Rating	A-/Stable	Affirmed
New York St Energy Research & Dev Auth (Long Island Lighting Co Proj) elec		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.