

**Rating Action: Moody's affirms Long Island Power Authority's (NY) A2 rating; assigns A2 to Series 2021 General Revenue Notes; Outlook stable**

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**Approximately \$4.5 billion of debt securities affected**

New York, January 11, 2021 -- Moody's Investors Service today affirmed the A2 rating assigned to the senior lien revenue bonds of Long Island Power Authority (LIPA or the Authority), NY and concurrently assigned an A2 rating to LIPA's planned issuance of \$250 million in Electric System General Revenue Notes, Series 2021. The rating outlook for LIPA is stable.

Proceeds from the Note offering will be used to fund costs related to Tropical Storm Isaias that severely impacted LIPA's service territory in August 2020. The estimated cost to repair damaged infrastructure and restore service to the approximate 645,000 customers who lost service during Isaias is \$300 million. The Authority will be seeking reimbursement from the Federal Emergency Management Agency ("FEMA") for up to 75% of these costs.

**RATINGS RATIONALE**

LIPA's A2 rating is supported by the utility's monopoly position as a provider of an essential service to large and diversified customer base with strong service area economic characteristics. With median household incomes and per capita metrics well above the national average the service area economy is arguably one of the strongest in the country and continues to be a positive factor underpinning LIPA's credit profile. Other positive credit factors include a suite of cost recovery mechanisms that support a stable and predictable cash flow profile and the utility's meaningful size and scale. These two considerations serve to provide resiliency to the utility's expected annual cash flow which has aided the growth in the utility's liquidity profile over the last several years.

The rating, however, is balanced by LIPA's highly leveraged balance sheet and financial metrics that are somewhat weak for the mid-A rating category. We calculate LIPA's average debt ratio at approximately 98% and its fixed obligation charge coverage (FOCC) ratio at around 1.20x in 2019. We understand that LIPA is projecting an FOCC for 2020 of 1.31x and that the Board of Trustees recently adopted several changes to LIPA's financial policy intended to enable the FOCC to reach 1.40x by 2022 and 70% debt ratio by 2028.

Today's rating action considers the impact to customer service and LIPA's reputation that surfaced following PSEG Long Island's delay in restoring electric service after Tropical Storm Isaias. Since 2014, PSEG Long Island, a wholly-owned subsidiary of Public Service Enterprise Group Incorporated (PSEG: Baa1 stable), has been LIPA's service provider pursuant to an Operating Services Agreement (OSA). The OSA provides PSEG Long Island broad control and responsibility for operating the utility, customer service, billing and collection, storm preparedness and service restoration. LIPA owns the utility assets and, as the owner, exercises contractual and statutory oversight over PSEG Long Island's operations.

LIPA's electric system operation is generally completed by 2,550 personnel within an entity called ServCo, a wholly-owned LIPA subsidiary, and managed by approximately 20 PSEG employees. For its service, LIPA pays PSEG Long Island a management fee which includes for incentives fees related to specified performance metrics. All of LIPA's operating and maintenance costs are paid by PSEG Long Island, primarily to ServCo employees, for which LIPA fully reimburses PSEG Long Island. In 2019, LIPA paid PSEG Long Island \$75 million in management fees and reimbursed \$580 million in operating expenses.

Since its formation, PSEG Long Island operations of LIPA's assets have been generally successful. A Task Force created to undertake an independent investigation into the failure of the utility's response after Isaias, however, attributed blame on PSEG Long Island's managerial oversight for various failures and made a recommendation, among other things, to LIPA's Board of Trustees to renegotiate or terminate the existing OSA. Termination is within the legal right of the Board of Trustees and a decision is expected in the first half of 2021.

Under a scenario whereby the Board of Trustees terminates the OSA, LIPA would retain ownership of ServCo

who would continue to maintain day-to-day operations of LIPA's assets albeit with different managerial oversight. Operating costs under this scenario would likely closely align with the current profile. While the outcome of these events remain unclear, we do not believe at this juncture that any change contemplated in the way service is provided to LIPA's customers could have negative rating implications.

#### RATING OUTLOOK

The stable outlook reflects LIPA's strong liquidity profile that is expected to remain in excess of \$1 billion.

#### FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

LIPA is reasonably positioned within its rating category and upward rating movement is not currently anticipated. A sustainable improvement in key credit metrics, such as fixed obligation charge coverage of 1.50x and a debt ratio below 80%, could give rise to a higher rating.

#### FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

Unexpected deterioration in key financial metrics, including fixed obligation charge coverage declining to below 1.20x on a sustained basis could trigger a negative rating action. To the extent that problems surrounding electric service restoration in a timely manner recur, it could have negative rating ramifications, especially if it results in political intervention.

#### LEGAL SECURITY

The 2021 Notes will be issued pari passu to all outstanding senior debt obligations of the Authority and are secured by the revenues generated by the operation of LIPA's electric transmission and distribution system with rate required to meet a 1.10x rate covenant. The note resolution contains a basic flow of funds including a Rate Stabilization Fund. The Authority is required in its bank covenants to at all times maintain on deposit in the Rate Stabilization Fund an amount not less than \$150,000,000. There is no debt service reserve fund, which we consider credit negative.

#### USE OF PROCEEDS

Proceeds from the note offering will be used to reimburse costs related to Tropical Storm Isaias. The Authority has sought reimbursement from the Federal Emergency Management Agency (FEMA). However, the Authority expects to make expenditures to pay costs associated with Tropical Storm Isaias in advance of any recovery from FEMA. Total costs associated with Isaias is \$300M and the anticipated recovery from FEMA is \$225M or 75%.

#### PROFILE

LIPA was established in 1986 as a corporate municipal instrumentality of the State of New York under the Long Island Power Authority Act (the LIPA Act). In 1998, the Authority became the retail supplier of electric service in most of Nassau and Suffolk Counties and the Rockaway Peninsula of Queens by acquiring the Long Island Lighting Company (LILCO). LIPA's assets currently consist of a transmission and distribution system that is used to serve approximately 1.1 million customers in an approximately 1,230 square mile service territory.

#### METHODOLOGY

The principal methodology used in these ratings was US Public Power Electric Utilities with Generation Ownership Exposure Methodology published in August 2019 and available at [https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC\\_1170209](https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1170209) . Alternatively, please see the Rating Methodologies page on [www.moodys.com](http://www.moodys.com) for a copy of this methodology.

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