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Ratings

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Summary:

Long Island Power Authority, New York; Retail Electric

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Credit Profile		
US$368.0 mil elec sys gen rev bnds ser 2021A due 12/31/2042		
Long Term Rating	A/Stable	New
US$194.0 mil elec sys gen rev bnds ser 2021C due 12/31/2042		
Long Term Rating	A/Stable	New
US$175.0 mil elec sys gen rev bnds (Mandatory Tender Bnds) ser 2021B due 12/31/2051		
Long Term Rating	A/Stable	New
Long Island Pwr Auth RETELEC		
Long Term Rating	A/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'A' rating to the Long Island Power Authority (LIPA), N.Y.'s proposed $368 million electric system general revenue bonds, series 2021A; $175 million electric system general revenue bonds, series 2021B; and $194 million electric system general revenue bonds, series 2021C. At the same time, S&P Global Ratings affirmed its 'A' rating on the authority's existing $4.8 billion of revenue bonds. The outlook is stable.

The authority plans to apply proceeds to fund system improvements and to refund portions of existing debt.

The 2021B bonds will be sold in a term mode. Although the 2021B bonds are subject to mandatory tender at the end of each term mode, at the option of management, or on any mode change date, we conclude the mandatory tender provisions will not impair liquidity because LIPA's obligation to purchase tendered bonds is contingent on its securing remarketing proceeds sufficient to fund the purchase of all tendered bonds.

The rating reflects the application of our "U.S. Municipal Retail Electric And Gas Utilities: Methodology And Assumptions" criteria, published Sept. 27, 2018. The rating incorporates an adjustment that reflects projections that include $2.7 billion of 2021-2024 capital projects, the potential costs of complying with New York State's ambitious plans to decarbonize the electric sector, and the operational uncertainties the utility faces as it revisits its contract that outsources the operations of the transmission and distribution system to address the operator's lengthy Hurricane Isaias service restoration times. In addition, the rating reflects those provisions of our "U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology And Assumptions" criteria, published Jan. 19, 2016, delineating S&P Global Ratings' methodology for assessing the impact of securitized debt.

Credit overview

LIPA is a corporate municipal instrumentality and political subdivision of New York State. The authority is among the three largest public power utilities in the U.S. by customers and revenues. It serves more than 1.1 million retail customers. The utility derives 54% of its revenues from residential customers and the balance from commercial and governmental customers. LIPA principally serves customers in Nassau and Suffolk counties, where income levels are about 50% above the national household effective buying income.

Unlike similar-sized peers, LIPA primarily relies on others to supply its customers' electricity needs, purchasing all but a small portion of its electricity from third parties. Moreover, from inception, New York State directed LIPA to outsource day-to-day operations and capital planning to a private company viewed as better able to provide reliable service. However, following 2012's Superstorm Sandy and 2020's Hurricane Isaias, the respective private contractors operating the transmission and distribution systems for LIPA during those weather events were unable to restore service within an acceptable time frame. Consequently, in fall 2020, the utility's board directed management to evaluate alternative arrangements for system operations because August's poor storm response once again raised questions about the effectiveness of the outsourcing model. We believe that outside contractors' recurring protracted service restoration times following storms highlights significant operational exposures that have the potential to negatively affect operational and financial performance. LIPA is in the process of renegotiating its contract with the current operator, PSEG-Long Island. In addition to needing to obtain its contractor's acquiescence to revisions, amending the contract also needs approvals from state officials.

LIPA's limited owned generation capacity consists of a 224-megawatt (MW), 18% interest in the Nine Mile Point 2 (NM2) nuclear plant, which equaled about 9% of 2020's retail energy requirements. 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 24% of LIPA's 2020 power supply. The cost of reserving National Grid capacity does not abate when LIPA purchases power from others, but LIPA can direct National Grid to remove generation and related capacity charges from the power supply agreement. 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.

The stable outlook reflects strong fixed charge coverage (FCC), the availability of several robust pass-through mechanisms for recovering rising costs, and favorable service area demographics that can support the utility's high rates.

Environmental, social, and governance (ESG) factors

Based on the utility's nuclear resource and purchases from predominantly gas-fired generation resources, we believe LIPA faces moderate environmental exposures. However, the service territory's extensive coastal exposure heightens susceptibility to storm damage attributable to climate change.

Although Energy Information Administration data show that LIPA's weighted-average retail rates were 17% above the state average in 2019, we believe that service territory income levels temper the social risks associated with this rate disparity, but also observe historical resistance to rate adjustments. Although customers' delinquent payments in 2020 reached $177 million due to the economic effects of the pandemic, we believe the state's moratorium on service disconnections depressed amounts the utility could record as uncollectible. Yet, uncollectible balances have consistently been below 1% of billed revenues. The utility can socialize uncollectible payments but doing so could place upward pressure on already high rates.

We associate governance risk with the utility because of the requirement that LIPA must litigate rate adjustments that seek to increase aggregate revenues by more than 2.5% per year. Moreover, unsatisfactory storm response times by two contractors raises questions about controls under outsourcing arrangements.

Stable Outlook

Downside scenario

If reliability does not improve following proposed revisions to LIPA's business model that outsources day-to-day operations and customer dissatisfaction weakens financial flexibility, we could lower the rating. Likewise, if funding for capital spending adds materially to unsecuritized debt and debt service and adversely affects financial margins or the use of securitized debt to fund capital improvements adds substantial costs to customer bills and reduces financial flexibility, we could lower the rating. We could also lower the rating if moratoriums on service disconnections for nonpayment meaningfully disrupt cash flows.

Upside scenario

We do not expect to raise the rating during the two-year outlook because the utility faces meaningful operational and financial exposures, including buttressing the performance of PSEG-Long Island, the presence of a sizable capital program, the uncertain costs of decarbonization, and the timing of collections of delinquent bills associated with the pandemic and its moratorium on disconnections.

Credit Opinion

LIPA reported $4.8 billion of short- and long-term debt as of Dec. 31, 2020. This debt balance is net of the $4.5 billion of debt it securitized to improve the financial cushion available to its unsecuritized bondholders. Although LIPA's financial statements consolidate the utility's 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, is not an obligation of the authority, and does 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 the UDSA. Consequently, our financial analysis removes UDSA-related revenues and debt service from our assessment of the LIPA debt obligations, but our analysis also explores the burden of high retail rates that capture on the same bill debt service on securitized and unsecuritized debt obligations, together with other revenue requirements. In August, New York State enacted legislation increasing the securitization bond authorization to $8 billion from $4.5 billion. Management anticipates using the additional authorization to refund portions of the existing securitization bonds and to also fund a portion of the utility's capital projects.

Our FCC calculation 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. FCC was 1.3x in 2018-2020, which we consider strong.

The utility recorded $1.2 billion of unrestricted cash and investments on its balance sheet as of Dec. 31, 2020, which we view as representing a strong five months' operating expenses. In addition, the utility maintains rate-stabilization funds subsumed within restricted assets. The audited financial statements do not delineate the balances held as rate-stabilization reserves.

LIPA principally serves customers in Nassau and Suffolk counties, where income levels are about 160% and 140% of the national household effective buying income, respectively, which we consider to be extremely strong. LIPA benefits from the stable revenue stream that more than 1.1 million customers provide. Residential customers provide about 54% of revenues, with commercial customers accounting for 42%, which we view as a favorable mix contributing to revenue stability. However, the utility is experiencing delinquent payments attributable to the economic effects of the COVID-19 pandemic and the state's moratorium on service disconnections.

Because customer bills include securitization debt service, converting portions of the debt portfolio to securitized debt has not reduced customer bills, which can influence ratemaking flexibility. Nevertheless, retail rates, inclusive of securitization charges, are competitive for the region, in our view, although they are high in absolute terms. Income levels contribute to affordability.

New York State's 2013 LIPA Reform Act transferred much of the day-to-day operating responsibilities to PSEG-Long Island, which is also responsible for capital planning. Under an operating agreement that expires in 2025, LIPA pays PSEG-Long Island an annual fee that contains performance-based incentives. The utility's contractual obligations to PSEG-Long Island include unfunded pension liabilities and other postemployment benefits relating to the PSEG-Long Island employees that serve the LIPA territory. The contractor's lengthy service restoration following Isaias evokes the inability of its predecessor to expeditiously restore customers' electric service following 2012's Superstorm Sandy. Customer ire following Isaias power outages triggered the board to direct management to revisit the incentives and penalties under the contract with PSEG-Long Island.

Unsatisfactory storm restoration responses by separate contractors in 2012 and 2020 raises questions about whether management negotiated contracts with system operators that adequately incentivize operators to counter the system's susceptibility to storm damage. It is uncertain whether proposed revisions to the PSEG-Long Island contract will drive consistently reliable electric service in storm-prone Long Island.

New York's Department of Public Service (DPS) must review rate proposals that seek to increase aggregate revenues by more than 2.5% per year. In our view, the rate-setting construct could reduce financial flexibility. The potential for rate oversight distinguishes LIPA from most other public power utilities. However, the several available pass-through and decoupling mechanisms could diminish the need for base-rate adjustments that exceed the threshold.

Like other regulated utilities, LIPA has not received guarantees it will achieve specific coverage metrics, but the several adjustment mechanisms the DPS included in its rate recommendation for addressing changes in prescribed variable costs should promote sound credit quality. The decoupling mechanism is a significant tool but not an absolute guarantee for insulating financial performance from variable electric sales and revenues. Moreover, the board amended the decoupling mechanism to allow the utility to defer portions of cost recovery to later periods.

In June 2019, New York enacted the Climate Leadership and Community Protection Act, directing the state's utilities to produce 100% of their electricity from carbon-free resources by 2040. We believe meeting these targets could stress the average cost of power supply, but the availability of pass-through and decoupling mechanisms directly tied to these initiatives should help facilitate a sound alignment among revenues, expenses, and debt service.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of September 13, 2021)		
Long Island Pwr Auth elec sys gen rev bnds ser 2008A dtd 10/16/2008 due 05/01/2033		
Long Term Rating	A/Stable	Affirmed
Long Island Pwr Auth RETELEC		
Long Term Rating	A/Stable	Affirmed
Long Island Pwr Auth RETELEC		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC		
Long Term Rating	A/Stable	Affirmed
Long Island Pwr Auth RETELEC (AGM)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (AGM)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (AGM)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (AGM)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (ASSURED GTY)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (BAM)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (BAM) (SECMKT)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (BAM) (SECMKT)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (BAM) (SECMKT)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (BHAC)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (BHAC) (SEC MKT)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed

Ratings Detail (As Of September 13, 2021) (cont.)		
Long Island Pwr Auth RETELEC (BHAC) (SEC MKT)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Long Island Pwr Auth RETELEC (CIFG)		
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 Pwr Auth) (MBIA) (National) (SEC MKT)		
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.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.