S&P Global Ratings

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Summary:

Long Island Power Authority, New York; Retail Electric

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Credit Profile		
US$144.095 mil elec sys gen rev bnds ser 2022A due 09/01/2044		
Long Term Rating	A/Stable	New
US$100.0 mil elec sys gen rev bnds ser 2022C due 09/01/2038		
Long Term Rating	A/Stable	New
US$100.0 mil elec sys gen rev bnds ser 2022B due 09/01/2052		
Long Term Rating	A/Stable	New
Long Island Pwr Auth RETELEC		
Long Term Rating	A/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'A' rating to the Long Island Power Authority (LIPA), N.Y.'s proposed $144.095 million electric system general revenue bonds, series 2022A; $100 million electric system general revenue bonds, series 2022B mandatory tender bonds; and $100 million electric system general revenues bonds, series 2022C mandatory tender bonds.
- At the same time, S&P Global Ratings affirmed its 'A' rating on the authority's existing $5.3 billion of revenue bonds.
- The outlook is stable.

Security

The authority pays debt service on its bonds from the revenues remaining after paying the operating expenses of the electric system.

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

The 2022B and 2022C bonds are multimodal bonds that are subject to mandatory tender on each mode change date. We conclude the mandatory tender provisions will not impair liquidity because LIPA's obligation to purchase tendered bonds is contingent on it securing remarketing proceeds sufficient to fund the purchase of all tendered bonds.

Credit overview

The rating reflects the strengths that a large, highly residential, and generally affluent customer base contribute to revenue stability and predictability, along with sound fixed charge coverage (FCC) and robust liquidity.

Tempering these strengths are projections that include $3.4 billion of 2022-2025 capital projects, the potential costs of complying with New York State's ambitious plans to decarbonize the electric sector, retail rates we consider high, and the operational uncertainties the utility faces as it revisits its contract that outsources the operations of the transmission and distribution system due to the operator's lengthy Tropical Storm Isaias service restoration times and the inadequacies of communications systems for fielding customer outage reports.

We assigned the rating applying our "U.S. Municipal Retail Electric And Gas Utilities: Methodology And Assumptions" criteria, published Sept. 27, 2018; and those provisions of our "U.S. Municipal Water, Sewer, And Solid Waste Utilities: Methodology And Assumptions," April 14, 2022, delineating S&P Global Ratings' methodology for assessing the impact of securitized debt.

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 about 1.2 million retail customers in Nassau and Suffolk counties where income levels are about 160% and 143% of the national household effective buying income, respectively. The utility derives 54% of its revenues from residential customers and the balance from commercial and governmental customers. We view the sizable revenue contributions from residential customers and the absence of substantial industrial loads as contributing to revenue stability.

In June 2019, New York enacted the Climate Leadership and Community Protection Act, directing the state's utilities to source 70% of their electricity from renewable resources by 2030 and 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.

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 its day-to-day operations and capital planning to a private company viewed as having expertise that would translate into 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 were unable to restore service within an acceptable time frame and communications systems were inadequate for fielding customer outage reports. Consequently, in fall 2020, the utility's board directed management to evaluate alternative arrangements for system operations, citing questions about the effectiveness of the outsourcing model.

As part of its response to 2020's protracted outages, LIPA has amended and restated its contract with system operator PSEG-Long Island (PSEGLI). The revisions impose higher performance standards on PSEGLI, including more substantial financial penalties for substandard performance. The authority is exploring whether to extend the PSEGLI contract beyond 2025, enter into a contract with another company to handle day-to-day operations, or bring these functions in-house.

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 11% of 2021'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. Yet, National Grid provided 32% of 2021's power supply, compared with 18% in 2017, as opportunities for economy purchases declined.

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.

Environmental, social, and governance

The combination of a nuclear resource that does not produce greenhouse gases and purchases from predominantly gas-fired generation resources exposes LIPA to moderate environmental risks. However, the service territory's extensive coastal exposure heightens susceptibility to storm damage attributable to climate change, which has a moderate negative influence on the rating.

Although Energy Information Administration data show that LIPA's weighted-average retail rates were 18% above the state average in 2020, we believe that service territory income levels temper the social risks associated with this rate disparity. However, we also observe historical resistance to rate adjustments, in part because of the perceived dissonance among high rates and lengthy storm outages. Customer bills include securitization debt service, 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.

Customers' delinquent payments in 2021 reached $207.2 million, compared with $177 million in 2020, due in part to the economic effects of the COVID-19 pandemic. In addition, we believe the state's moratorium on service disconnections during the pandemic depressed amounts the utility could record as uncollectible. Charge-offs declined to 0.28% of revenues in 2021 from 0.73% in 2017. 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. However, LIPA's base-rate adjustments have not triggered this threshold in 2019-2022 and management believes it will not do so in 2023. In addition, the several available pass-through and decoupling mechanisms could diminish the need for base-rate adjustments that exceed the threshold.

In addition to the governance risks we associate with potential exposure to rate oversight, the unsatisfactory storm response times by two contractors in past storms raises questions about controls under outsourcing arrangements. Whether revisions to the contract with PSEGLI that impose higher performance standards on the contractor will reduce operating risks remains untested.

Outlook

The stable outlook reflects favorable FCC, the availability of several robust pass-through mechanisms for recovering rising costs, and service area income levels that can support the utility's high rates.

Downside scenario

We could lower the rating if reliability does not improve and customer dissatisfaction weakens financial flexibility. 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 or if the socialization of uncollectible accounts reduces financial flexibility.

Upside scenario

We do not expect to raise the rating during the two-year outlook because we believe the utility faces meaningful operational and financial exposures, including unresolved questions about whether LIPA or others will manage day-to-day operations, 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.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of August 5, 2022)		
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 (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 (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 (CIFG)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.