

Fitch Rates Kansas City BPU Bonds 'A+'; Outlook Stable

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NEW YORK--([BUSINESS WIRE](#))--Fitch Ratings has assigned an 'A+' rating to the Unified Government of Wyandotte County/Kansas City Board of Public Utilities (BPU) approximately \$115.8 million utility system improvement revenue bonds series 2016-A.

Fitch has also affirmed the 'A+' rating on the following outstanding BPU bonds:

--\$522.5 million utility system improvement revenue bonds.

The Rating Outlook is Stable.

Bond proceeds will be used to fund environmental capital expenditures at BPU's Nearman coal-fired generating station. The bonds are expected to price on January 13, 2016.

SECURITY

The bonds are payable from net revenues of the combined electric and water system on parity with outstanding utility system revenue bonds (senior lien).

KEY RATING DRIVERS

COMBINED UTILITY SYSTEM: The Kansas City Board of Public Utilities (BPU) provides retail electric and water services in a largely overlapping service area. The vertically integrated electric system provides approximately 84.3% of the combined utility system's operating revenues.

STABLE FINANCIAL PERFORMANCE: Financial metrics for 2014 were generally in line with rating category medians with Fitch-calculated debt service

coverage, adjusted for BPU's high payment in lieu of taxes (PILOT), at 1.49x and liquidity at 73 days cash on hand. Metrics for 2015 are expected to be in-line with recent performance.

FLEXIBLE RATE STRUCTURE: BPU's rate structure is viewed as a credit positive with an energy cost charge that is adjusted on a quarterly basis and an environmental surcharge that is reset annually to cover debt service costs related to the utility's environmental compliance projects. The utility has demonstrated an ability to increase base rates by gradually raising rates through a multiyear plan that culminated in 2013.

TRANSITIONING POWER SUPPLY: The utility is undergoing a significant transition in its power supply as it moves away from older vintage coal-fired plants towards a greater reliance on natural gas-fired and renewable resources. The transition is largely driven by environmental regulations requiring additional pollution controls on the system's coal-fired power plants.

WEAK SERVICE AREA: The 'A+' rating takes into account the service area's below-average wealth indicators, large commercial and industrial customer base, and relatively flat sales growth. Rating concerns are mitigated by improving economic trends and an only moderately concentrated customer base.

RATING SENSITIVITIES

MAINTENANCE OF FINANCIAL METRICS: The rating reflects the Kansas City Board of Public Utilities' demonstrated ability and willingness to raise rates and modify its rate structure to maintain financial metrics commensurate with 'A+' rated public power utilities. An unexpected reversal from this practice, particularly given the system's significant capital needs, could likely pressure financial performance and could lead to negative rating action.

CREDIT PROFILE

BPU is a combined electric and water utility system serving approximately 63,000 electric and 50,000 water customers. The utility's electric system is an integrated system consisting of generation, transmission, and distribution assets.

Approximately 84.3% of BPU's revenue is derived from the electric system, with the balance coming from the water system. Sales to commercial and industrial customers account for about 61% of combined utility system revenue, with residential customers accounting for approximately 23%.

TRANSITIONING POWER SUPPLY

As a utility that derived 88% of its 2013 energy from older vintage coal-fired units, BPU is exposed to environmental regulations promulgated by the U.S. Environmental Protection Agency (EPA), including Mercury and Air Toxic Standards (MATS). Following a strategic review, BPU is executing a plan aimed at meeting air quality standards and reducing dependence on coal and transitioning towards greater use of natural-gas fired and renewable resources.

The first step was completed in December 2012 with the acquisition of a 17% ownership interest (110 MW) in the Dogwood Generating Facility, an efficient combined cycle gas-fired power plant. The next phase in BPU's compliance plan was completed in April 2015 with the permanent conversion of its Quindaro units one and two to natural gas from coal. The next step and cornerstone of the project is a \$250 million capital investment at the 257 MW Nearman Station to bring the plant into compliance with air quality standards by 2017. A portion of these costs will be financed by proceeds of the series 2016 bonds.

BPU has a robust capital improvement plan with approximately \$497 million of investments planned between 2016 through 2020. A significant portion of the plan is tied directly to BPU's strategy of fuel diversification and environmental compliance. Management has stated that an additional debt issuance of approximately \$60 million is expected mid-2016 with another potential financing for around \$50 - \$70 million in 2018 or later.

STABLE FINANCIAL PERFORMANCE

BPU's debt service coverage levels are stable with Fitch calculated coverage remaining above 2.18x over the past five years. Fitch calculated coverage was 2.22x in 2014 and 1.49x after adjusting for the system's relatively high PILOT amount, which is paid on a monthly basis. Financial projections for 2015 show

Fitch-calculated debt service coverage levels, adjusted for PILOT expenses, at similar levels to 2014.

BPU's financial performance has remained relatively stable since 2010 following a period of volatility during the recession, particularly in 2008 and 2009 when BPU's commercial and industrial volumes were adversely affected and PILOT payments to the Unified Government were increased. The improved performance since 2009 was largely driven by a multiyear rate plan that was fully implemented in 2013.

Liquidity levels increased to 73 days cash on hand at the end of 2014, a significant improvement from just 19 days cash on hand at the end of 2008. Additional gains are expected as management has increased their informal target to 80 days cash from the previous 50. As of September 30, 2015, BPU had 104 days cash on hand.

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria

Revenue-Supported Rating Criteria (pub. 16 Jun 2014)

https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=750012

U.S. Public Power Rating Criteria (pub. 18 May 2015)

https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=864007

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form

https://www.fitchratings.com/creditdesk/press_releases/content/ridf_frame.cfm?pr_id=997385

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