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Ratings

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Summary:
Bountiful, Utah; Retail Electric

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Table Of Contents

Summary:

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Credit Profile		
Bountiful elec (AGM)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rationale

S&P Global Ratings has affirmed its 'A+' underlying rating (SPUR) on the City of Bountiful, Utah's $16.5 million series 2010 electric revenue bonds (federally taxable-issuer subsidy-recovery zone bonds). The outlook is stable.

The rating reflects our opinion of the light and power department's:

- Stable and diverse customer base, with above-average income levels, and the city's convenient location just 8 miles from Salt Lake City;
- Competitive rates; and
- Historically strong coverage and liquidity levels.

Partially offsetting the above strengths, in our view, is the department's relatively small size, which exposes it to fluctuations in revenues and expenditures.

The business profile score is '4' on a scale of one to 10, with '1' being the strongest score attainable. The business profile represents the department's competitive rates, stable economic base in its service territory, and low operational risk given the mostly transmission-and-distribution nature of the city's electric system. These factors are offset by the system's relatively small size and projected dip in liquidity coverage, although projections are based on conservative assumptions.

Net revenues of the city's light and power department secure the bonds.

Bountiful has a population of 43,651 (in 2016) and its light-and-power system serves 16,800 customers, of whom 92% are residential. The department's revenues and sales are also primarily residential (58% and 55%, respectively), which in our view represents a stable customer base, but there is a slight exposure to commercial customers, which comprise about 34% of both revenues and sales. The system serves a 14-square-mile area coterminous with the city, about 8 miles north of Salt Lake City. The city is the main retail and regional hub for south Davis County, and is easily accessible by Interstate 15. Bountiful's unemployment rate was 3.3% in 2016, and its median household effective buying income was 24% above the U.S. national average--which we believe is demonstrative of a stable local economy.

The department's customer base is not concentrated, with the 10 leading customers representing 23% of total operating revenues in 2017. The leading customer, Air Products Corp., represented 9% of total operating revenues. Management is unaware of any cutbacks or expansions among its top customers.

The system includes 230 miles of distribution-and-transmission lines, eight substations, and a 26-mile line to the city-owned Echo Hydroelectric Project. The department derives its energy supply from several sources, including contracts for 16-26 megawatts (MW) of power from the Colorado River Storage Project through 2024 (39% of its energy supply in fiscal 2017) and firm power purchases acquired through Utah Associated Municipal Power Systems (UAMPS) through 2022 (31% of its energy supply in fiscal 2017). It also has power sales agreements for zero to 30 MW of coal-based power from Utah's Intermountain Power Project (IPP) through 2027, via its membership in UAMPS and 5 MW of coal-based power from the San Juan Unit No. 4 in New Mexico through 2045. The city is not currently purchasing power from IPP, but San Juan coal-fired energy represented 12% of the department's energy in 2017. Other owned generation includes 32.3 MW from its own gas-fired plant, 4.5 MW from the Echo Hydroelectric Project, and 1.8 MW from the Pineview Hydroelectric Project. Spot-market purchases accounted for 8% of power supply in 2017.

According to management, 47% of resources (all hydro) were non-carbon emitting in 2017, but do not currently meet the state's definition for eligible renewable. Utah has a renewable portfolio standard of 20% by 2025. The department is working to get its Echo project counted as an official renewable resource, because of the improvements it has made with the Bureau of Reclamation. A small portion of the department's net metering program is also qualified as renewable energy. The department is looking at a few wind and solar projects to add to its resource portfolio in the coming years. It is also working with UAMPS on a nuclear project on the National Laboratories site near Idaho Falls, Idaho. UAMPS and NuScale have agreed to install a modular-designed reactor on the site. The department is looking for another participant to engage in this project, which management believes will likely cause delays.

Bountiful reviews rates annually during the budget process. The U.S. Energy Information Administration weighted average system rate versus the state rate was 96% in 2015, which we consider competitive. The department did not increase rates from 2014-2016, but it did raise its customer charge in fiscal years 2017 and 2018 by 1.5% and 3%, respectively, to fund capital projects. The city has no plans to raise rates, although management acknowledged it could increase rates to support its five-year capital improvement plan (CIP).

The city aims to fund its $22.2 million CIP (annual expenses of between $2.6 million and $6.2 million) mostly through surplus revenues, unrestricted cash on hand, and, if necessary, future rate increases. Unrestricted cash totaled $27.2 million in fiscal 2017, equal to 490 days of operations, and this includes the city's $5.3 million balance in its rate stabilization fund. The conservative, in our view, 2018 budget and 2019-2022 projections show cash gradually decreasing to $12.6 million, with the inclusion of planned annual capital expenditures. Overall, we view the department's liquidity position as very strong, and conservative budgeted and projected cash sufficient even after accounting for future annual CIP expenses.

Fixed-charge coverage, our measure of the ability of net cash from operations to cover both on- and off-balance-sheet fixed-charge obligations, was approximately 1.3x in 2017, a level that we consider good. The off-balance-sheet obligation reflects the department's capacity payments associated with purchased power, as well as annual transfers. Based on management projections, we calculate fixed charge coverage to decline to about 1.1x after 2017; however based on the department's track record of outperforming historical projections and conservative elements such as a lack of rate increases, conservative projected power and generation expenses, and no growth in customers, we believe the projected decline in liquidity and coverage metrics is not plausible.

Bountiful has a very low debt burden, with debt to capitalization of 15% in 2017 and has no plans to issue additional debt in the future.

Outlook

The stable outlook reflects our expectation that, over the next two years, the department will continue to adjust rates as needed to maintain strong financial margins and fund ongoing capital needs.

Upside scenario

We do not expect to raise the rating during the two-year outlook period due to the department's capital needs that could result in a decline in liquidity. In addition, the department's small size exposes it to fluctuations in revenues and expenditures.

Downside scenario

We could lower the rating if capital-spending needs accelerate, operating costs increase, or projections come to fruition and the department does not raise rates or adjust for capital costs to prevent material erosion of coverage and liquidity.