MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns A2 rating to SFP Transmission, NY's inaugural bond offering; outlook is stable

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Approximately $569 million of debt securities affected

New York, March 21, 2022 -- Moody's Investors Service has assigned an A2 rating to New York State Power Authority's $569 million Green SFP Transmission Project Revenue Bonds, Series 2022A due November 2061. The rating outlook is stable.

SFP Transmission has been formed by the New York Power Authority (NYPA: Aa2) to finance, operate, and maintain transmission projects that are eligible to collect transmission revenue through the New York Independent System Operator (NYISO). SFP Transmission has been structured to be a separate credit from NYPA 's general credit with the repayment of SFP Transmission's debt obligations derived solely from and secured by a pledge of revenue earned by the specific transmission projects' assets. Prospectively, NYPA may fund additional transmission investments with incremental SFP Transmission bond offerings subject to obtaining approval for regulated cost recovery from the Federal Energy Regulatory Commission (FERC) and designating such projects as SFP Transmission projects.

Today's rating assignment will not have negative implications for NYPA's overall credit profile in that NYPA's standalone credit profile will benefit from the residual cash flows it expects to receive each year after the repayment of SFP Transmission's debt service.

Proceeds from the bond offering will be used to fund capital expenditures related to two transmission projects currently under construction, the Central East Energy Connect Transmission Project (CEEC) and the Smart Path Reliability Transmission Project (Smart Path).

RATINGS RATIONALE

The A2 rating considers the stable and predictable cash flow profiles of the transmission projects that will support SFP Transmission's long-term debt repayment profile and the important role of the assets towards achieving New York State's clean energy and electric reliability goals. Revenues from the two transmission projects should provide predictable cash flow leading to strong and stable debt service coverage ratios at SFP Transmission. The current rating is constrained to some degree by construction and execution risk as these projects represent NYPA's initial financing using the SFP Transmission structure.

While construction risk is aided by the existence of fixed price contracts, the receipt of the necessary permits, plus incremental downside protection from a rate recovery standpoint, the current global macroeconomic conditions do pose a risk for the timing and the related budget for large construction projects owing to underlying inflation expectations and the potential for supply chain constraints. Additionally, the rating considers the uncertainty at this juncture around the contribution of future transmission projects to SFP Transmission and the implications it could have on SFP Transmission's prospective financial profile as we anticipate incremental construction projects being regularly added over the next several years. That said, the rating is strongly positioned within the A rating category owing to the anticipated cash flow generation from the two projects coupled with the protection afforded to the projects under certain downside scenarios.

Notwithstanding the standalone nature of the pledge and the non-recourse nature of the obligation to the NYPA General Resolution, the A2 rating further recognizes the benefits of the assets being owned by NYPA, an experienced utility operator. The Authorization for NYPA to issue SFP Transmission obligations was granted in NYPA's General Resolution dated December 7, 2021. According to NYPA's General Resolution, separately financed projects such as the ones under SFP Transmission will not receive any support from NYPA's general credit, must be self-supported by pledged revenues, and pay for its own costs of operations. Moreover, there will be no cross default between the two entities. Repayment of SFP Transmission's debt obligations is derived solely from and secured by a pledge of the revenues earned from its assets. Because of these considerations in establishing SFP Transmission along with its continuing ownership by NYPA, governance is considered a key consideration in this rating action.

CEEC is designed to increase electric transmission from Central to Eastern New York. It is approximately 36% complete (anticipated commercial operations in late 2023) and ownership is split between NYPA (37.5%) and an unaffiliated third-party (62.5%). Construction for the project will be managed by the unaffiliated third-party company. In contrast, NYPA is the sole owner of Smart Path, a project focused on providing transmission congestion relief and improved electric reliability. It involves rebuilding transmission lines that extend approximately 86 miles from the St. Lawrence Power Project's Robert Moses Power Dam Switchyard to the Town of Croghan, Lewis County, NY and consists of 6 separate segments, 3 of which have been completed (about 64% complete) with full operation anticipated in mid-2023. Because of the straightforward nature of the Smart Path project which includes rebuilding transmission assets in existing rights of way, the progress to date, and the fact that the project's construction does not involve an unaffiliated third party, we view construction and execution risk at Smart Path to be lower than at CEEC.

NYPA's combined budgeted cost for the two transmission projects is $694 million ($210 million for CEEC and $484 million for Smart Path). NYPA's equity contribution is expected to be equal to 10% of the projected total cost of the two transmission projects.

As discussed, rate recovery for each of the two projects will occur through FERC regulated rates, a construct that we view as credit supportive and resilient under a number of scenarios. While the FERC approved rate treatment differs slightly between the two transmission projects and both recovery mechanisms are different than the recovery framework in place for NYPA projects under the General Resolution, the combined revenue profile is expected to be stable and predictable, and is a critical rating consideration. Specifically, the aggregate annual revenue run rate of the transmission projects under a base case financial scenario is in excess of $60 million through at least 2036 and structured to provide annual debt service coverage (DSC) that averages slightly more than 1.6 times annually through debt maturity scheduled in 2061.

Rate treatment for CEEC provides protection against construction delays, including an allowed return during construction and 100% cost recovery in the event of project abandonment that is outside of NYPA's reasonable control. Moreover, in the event of cost overruns, a FERC approved cost containment provision allows 80% of CEEC's cost above the pre-determined cap to be recovered at the FERC approved base return on equity and 20% of the costs above the cap to be recoverable at the cost of debt.

The rate recovery treatment for Smart Path is less robust but remains resilient. While no cost recovery occurs during construction, AFUDC accumulates with cost recovery beginning when a segment is placed in-service. To date, 3 of the 6 Smart Path segments are in-service providing current cash flow for SFP Transmission, with full project completion expected by mid-2023. The Smart Path Project will receive revenue as an NTAC project under NYPA's formula rate including an all-in ROE of 9.45% based on a assumed debt to equity of 1:1. Recovery of any cost in excess of the approved budgeted amount will require approval from the majority of the transmission owners operating in New York.

External factors that provide protection against construction delays and cost overruns include fixed price Engineering, Procurement and Construction (EPC) contracts with competent contractors, construction progress made to date and contingency amounts build built into the approved budgets. That said, our analysis considered various financial sensitivities, including cost overruns. Annual debt service coverage under stressed scenarios suggest annual DSC in excess of 1.5 times.

Structural Features

Structural considerations include a debt service reserve requirement equal to the three pronged test (lesser of maximum annual debt service, 10% of proceeds, or 125% of average annual debt service), the application of revenues through a waterfall of accounts and limitations on the withdrawal of funds. Moreover, the issuance of parity debt requires the issuer to meet certain requirements, including minimum historical and projected debt service coverage.

The bonds will be payable solely from the net revenue of the designated transmission projects and will be supported by dedicated SFP Transmission liquidity and operating reserves. It will be legally separate from NYPA with no access to NYPA's liquidity and a SFP Transmission default would not cross-default to NYPA's General Resolution Bonds. In the event that NYPA were to default, SFP Transmission bondholders would not have acceleration rights. Instead, NYPA covenants to make all of the SFP Transmission's books and accounts available to the Trustee for the benefit of the SFP Transmission bondholders, and to pay the Trustee all of the SFP Transmission revenues, keeping the two pledges separate.

RATING OUTLOOK

The stable outlook considers construction progress made to date and reflects an expectation that both transmission projects will achieve operations in 2023 and produce cash flows that are aligned with the base case expectations.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATING

- Expectations for the commercial operations of CEEC and Smart Path being completed within the parameters of the current construction timeline and budget in a manner that supports the current projected base case financial performance.

- Greater clarity around the contribution of future transmission projects which together with the existing projects continue to support base case financial performance.

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATING

- Material cost overruns or sustained construction delays at either project which substantially increase the costs and substantially extend the timing for completion could lead to downward rating pressure.

LEGAL SECURITY

The bonds will be payable solely from the net revenue of the designated transmission projects and will be supported by dedicated liquidity and operating reserves. The bonds will be legally separate from NYPA's General Resolution with no access to NYPA General Resolution's liquidity and a SFP Transmission default would not cross-default to NYPA's General Resolution Bonds. Additional parity debt requires a certificate from NYPA that the obligations are eligible or expect to be eligible to be recovered under a FERC (or other relevant regulatory body) approved tariff, and must meet historic and pro-forma 1.2x DSC test. Rates must be sufficient to meet a 1.2x DSC requirement on an ongoing basis but the failure to meet such a requirement is not an event of default so long as NYPA, among other things, retains a rate consultant. A Debt Service Reserve Fund will be funded by a deposit of a Municipal Bond Debt Service Reserve Insurance Policy issued by Assured Guaranty in an amount equal to the lesser of (1) 10% of bond proceeds (2) the maximum Debt Service due in any fiscal year or (3) 125% of the average of the annual installments of Debt Service. Additionally, an operating reserve account funded equal to 50% of annual budgeted operating expenses will be established to fund repairs or replacements.

USE OF PROCEEDS

Proceeds from the bond offering will be used primarily to fund capital expenditures related to two transmission projects currently under construction, the CEEC Project and the Smart Path Project.

PROFILE

SFP Transmission is being established by NYPA to finance, operate, and maintain transmission projects that are eligible to collect transmission revenue through the NYISO.

METHODOLOGY

The principal methodology used in this rating was Regulated Electric and Gas Networks published in March 2017 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1059225 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

The rating has been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288235 .

At least one ESG consideration was material to the credit rating action(s) announced and described above.

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