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Omaha Public Power District, Nebraska; CP; Retail Electric

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Credit Profile		
US$100.0 mil elec sys rev bnds ser 2015B due 02/01/2027		
Long Term Rating	AA/Stable	New
US$100.0 mil elec sys rev bnds ser 2015A due 02/01/2045		
Long Term Rating	AA/Stable	New
Omaha Pub Pwr Dist elec		
Long Term Rating	AA/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services has assigned its 'AA' rating to the Omaha Public Power District (OPPD), Neb.'s electric system revenue bonds series 2015A and 2015B. At the same time, Standard & Poor's affirmed its 'AA' rating on OPPD's senior-lien electric system revenue bonds, its 'AA-' rating on the utility's subordinated obligations, , and its 'A-1+' commercial paper rating on the utility. The outlook is stable.

Our view of the following factors supports the ratings:

- A diversified customer base, with low customer concentration, and a service area with good economic characteristics;
- Historically reliable and low-cost power supply;
- Unregulated rate-setting ability with no expected retail-level competition;
- Strong coverage of debt service and fixed charges, and solid liquidity; and
- A moderate debt burden.

We believe the following factors offset these credit strengths:

- Although OPPD's Fort Calhoun Station (FCS) nuclear unit returned to service after a flood and electrical fire idled the unit for more than 2.5 years, the district incurred significant costs it is recovering over extended periods so as to minimize the rate impact. In addition, the extended outage (some of which is attributable to needing to gain Nuclear Regulatory Commission [NRC] approval to restart operations) and the related costs, demonstrate the risks associated with nuclear energy.
- OPPD has a substantial carbon footprint, and is exposed to adopted and announced Environmental Protection Agency (EPA) regulatory measures. The district has announced plans to retire, retrofit, or repower several coal units; significantly expand its demand side management (DSM) program; and double its renewable energy. Management expects that the retrofit costs and rate impact will be modest, and that its fuel mix will improve (by 2018) to an approximate balance of coal, nuclear, and renewable energy. However, we expect the district will remain exposed to costs associated with the regulation of greenhouse gas emissions at existing units. The EPA released its draft regulation June 2, 2014; we do not know the cost associated with the regulation and have not factored its potential impact into the rating.
- OPPD has a sizable $1 billion, five-year capital plan that could increase by more than $400 million if the EPA

determines that additional environmental controls are necessary.

The district's business position is '4' on Standard & Poor's '10'-point scale, with '1' the least vulnerable. Although the business position is solid, in our view, it reflects the above-mentioned operating risks. Despite this, Nebraska's favorable regulatory environment, OPPD's strong management team, and the depth and diversity of the utility's service area continues to support the business position.

Series 2015A bond proceeds will fund the district's capital plan. Series 2015B bond proceeds will refund debt outstanding.

OPPD has managed through increased operating and capital costs associated with a prolonged outage at its Fort Calhoun Nuclear Station. The outage cost the district $341 million in replacement power, operations and maintenance (O&M), and capital costs. Despite these costs, Standard & Poor's believes that OPPD still maintains solid coverage and liquidity. Management's projections suggest that the district expects this trend to continue, and we believe that the projections are based on reasonable assumptions for growth and future rate increases.

OPPD has a substantial carbon footprint -- 78% of total energy for retail sales was coal-based in 2013 (albeit at a heighted level with FCS out of service). As such, the district faces an array of regulatory measures that are forcing management to make difficult choices regarding its power supply. OPPD has announced the following plans to:

- Retire North Omaha Station (NOS) units 1-3 (300 megawatts [MW]) by 2016
- Retrofit NOS units 4 and 5 (349 MW) with activated carbon injection (ACI) and dry sorbent injection (DSI) by 2016
- Retrofit Nebraska City unit 1 (652 MW) with ACI and DSI by 2016
- Repower NOS units 4 and 5 with natural gas by 2023
- Expand DSM efforts

The NOS 1-3 units are small, old, and less efficient than other OPPD generating assets, and they are infrequently dispatched. Insofar as the district has excess capacity and no resultant base-load needs, management projects that these efforts will have a modest rate impact. We expect these actions to bring OPPD into compliance with the EPA's Mercury and Air Toxics Standard and Cross State Air Pollution Rule. However, the agency is assessing whether the fixes are sufficient to comply with its New Source Review requirements; should it issue an adverse decision, the district would need to install more costly controls, estimated at $418 million, which would ultimately have a more significant impact on ratepayers.

On June 2, 2014, the EPA released its draft regulation calling for a 30% cut in carbon dioxide emissions from the nation's existing power plants by 2030, with interim reductions covering the 2020-2029 timeframe. However, individual state reduction target vary; Nebraska expects to cut its carbon dioxide emission level by 26%. Utility-level reduction targets will not be known until the state submits to the EPA an implementation plan, which it must file by June 2016.

We believe it is too early to determine the impact of the regulation on credit quality. The draft rule could change significantly before being finalized in June 2015. The regulation is also almost certain to face litigation. In addition, state implementation plans need to be developed, the details of which will frame the challenges that utilities will face. Moreover, utilities will have an opportunity to formulate response strategies. As these issues come into focus, Standard

& Poor's will evaluate the challenges and assess the extent to which the response affects OPPD's credit quality.

In our opinion, the district's service area and customer base are credit strengths. OPPD provides retail service to about 356,000 customers in Omaha and the surrounding area in a state served exclusively by public power entities. The regional economy fared well through the recession, and Omaha's unemployment rate stands well below the national rate. Per capita personal income levels are good, in our view, at 105% of the national average. In addition, population growth has approximated the national average. Both of these suggest a degree of rate raising flexibility. The utility's user base is what we consider diverse, with the top 10 customers accounting for 14% of retail revenue. All industrial customers account for just 20% of operating revenue, a low level that we view as supporting credit quality. The three largest industries in the service area -- food and grain processing, medical and educational institutions, and insurance and other services -- are relatively stable businesses.

Off-system sales have been a significant and long-term source of revenues. They accounted for 19% of operating revenue in 2010, but only 11% in 2013 as the utility had less energy for resale with FCS offline. Given OPPD's favorable cost profile, the utility has continued to produce solid margins on market sales, which we note has not been the case for many utilities in the region because low natural gas prices and surplus energy have depressed electricity prices. The district's off-system sales are primarily off-peak sales of surplus power from base-load plants. Except for some market price exposure, OPPD does not assume large business risks associated with these wholesale energy sales, as the sales are contingent upon plant and system availability, thereby avoiding the risk of having to source power elsewhere when the plants are not operating.

The district's competitive positioning is what we view as favorable. We believe that the management's demonstrated willingness to raise rates when necessary to preserve both solid liquidity and a healthy coverage of fixed costs continue to support the ratings, and we do not believe that the change in competitive position will be significant enough to produce a change in credit quality. According to the Department of Energy's Energy Information Administration, OPPD's average revenue per kilowatt-hour was 6% below the state average in 2013, the most recent year of available comparative information, providing the district with modest rate-setting flexibility. We expect that the costs associated with the FCS outage will affect rates as they are recovered; OPPD has proposed aa 1.6% base-rate increase in 2015.

We believe the district's financial profile is a credit strength, with strong and steady coverage of both debt service and imputed debt costs associated with power purchases. OPPD manages to a 2x coverage target for all debt. Coverage of fixed obligations, which includes imputed debt service associated with power purchases and treats payments in lieu of taxes as an operating expense, has exceeded 1.75x in each of the past four years. The district projects coverage levels to remain near or above these levels during the next five years.

OPPD maintains what we view as solid liquidity. At fiscal year-end 2013 (Dec. 31), total liquidity measured about $410 million, representing about 195 days of operating expenses. The five-year financial forecast expects to maintain liquidity at or above 100 days of operating expenses, which we consider solid and supporting the rating.

We rate the district's short-term debt 'A-1+', reflecting the long-term rating, adequate liquidity, and access to the capital markets. Under a board adopted resolution, OPPD is authorized to have outstanding, at any time, up to $150 million of commercial paper. It has obtained a general line of credit from Bank of America N.A. for $250 million to provide liquidity supporting its commercial paper program, and to provide liquidity for other general expenditures. The district has covenanted to maintain sufficient undrawn on capacity on the line to cover all outstanding commercial paper. The line expires Oct. 1, 2015. OPPD's commercial paper has a subordinate lien on the revenue of its electric system.

Debt levels have edged upward over the past few years due to improvements at Fort Calhoun and the construction of the 682 MW Nebraska City 2 (NC2) unit, in which the district has a 50% share of the output. Seven public power entities in Nebraska, Missouri, and Minnesota take the remaining output under 40-year, take-or-pay, purchased power agreements. We expect that, net of issuance for participant shares of NC2 debt, debt-to-capitalization will be about 50% in fiscal years 2014-2018, despite a sizable $1 billion capital expenditure program. Capital costs could be about $418 million higher if scrubbers are required on NC1 if the EPA determines that they are necessary to comply with its New Source Review requirements.

Outlook

The stable outlook reflects Standard & Poor's expectation that financial performance will remain strong, and that wholesale sales will continue to be structured in a way that limits OPPD's financial exposure to volatile markets. Standard & Poor's expects that the district will raise rates as necessary in order to maintain its sound financial performance as it recovers operating costs associated with FCS and addresses environmental regulations. Further problems with FCS or a failure to make timely and sufficient rate increases could stress the ratings. Upward rating potential is not significant during our two-year outlook period, given the risks from OPPD's operating profile.

Fort Calhoun Nuclear Station

In June 2011, the Missouri River crested, causing widespread flooding in the Omaha area, impacting both the Fort Calhoun nuclear station and Nebraska City coal station. Fort Calhoun, which had been in the midst of a refueling outage. Following the flood, a fire in an electrical switch room and several adverse findings prompted the NRC to place FCS under its Multiple/Repetitive Degraded Cornerstone. The district satisfied the list of actions listed in under NRC 0350 in December 2013, and the unit is back in service, although the plant remains under 0350 status pending further inspections. Exelon Corp., the nation's largest nuclear operator, operates the plant under a 20-year agreement with OPPD. The outage resulted in $156 million in replacement power costs (up from $89 million estimated in 2013), $139 million in nonfuel O&M, and $46 million in capital costs. The district met the bulk of these costs with current cash, insurance proceeds, and available reserves. It is recovering the replacement power costs over a three-year period (2014-2016) via the fuel and purchased power cost adjustment mechanism. It has classified nonfuel O&M costs as a regulatory asset, with associated revenue recognized and expenses amortized across 10 years beginning in 2014. OPPD has also identified certain improvements to the FCS containment structure that are unrelated to the outage; management estimates the cost at $70 million, and plans to complete work during the scheduled 2015 and 2016 refueling outages. Fort Calhoun's license expires in 2033. Management is reassessing whether to pursue a 75 megawatt (MW) uprate ($300 million estimated cost) for FCS in 2019. OPPD has signed a purchased power agreement for energy associated with 400 MW of wind capacity placed into operation in 2017. With this addition, we expect renewable energy to supply 30% of the retail sales, and lower the district's carbon intensity.

Related Criteria And Research

Related Criteria

- USPF Criteria: Electric Utility Ratings, June 15, 2007
- USPF Criteria: Commercial Paper, VRDO, And Self-Liquidity, July 3, 2007
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011

Related Research

- U.S. State And Local Government Credit Conditions Forecast, Oct. 15, 2014

Ratings Detail (As Of November 21, 2014)		
Omaha Pub Pwr Dist elec sys subord program		
Long Term Rating	AA-/Stable	Affirmed
Omaha Pub Pwr Dist elec sys subord (wrap of insured) (FGIC & BHAC) (SEC MKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Omaha Pub Pwr Dist elec (MBIA) (National)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Omaha Pub Pwr Dist elec (PIBs) ser 2005A (wrap of insured) (FGIC) (National) (BHAC) (SEC MKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Omaha Pub Pwr Dist CP Program		
Short Term Rating	A-1+	Affirmed
Omaha Pub Pwr Dist elec sys		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.