FitchRatings

Public Finance
Public Power
United States

Arkansas River Power Authority, Colorado

The affirmation of Arkansas River Power Authority's Long-Term Issuer Default Rating at 'BBB–' reflects the utility's 'bbb' financial profile assessment, including an elevated leverage ratio of 10.9x in fiscal 2021, as measured by net adjusted debt to adjusted funds available for debt service. ARPA's leverage remains elevated since the issuance of approximately $156 million of debt during fiscals 2007, 2008 and 2010 to fund the Lamar Repowering Project (LRP). The LRP was decommissioned in 2014 due to the project's inability to meet emission requirements.

The rating also reflects the authority's strong revenue defensibility and strong operating risk profile. ARPA's revenue defensibility is derived from all-requirements long-term wholesale power supply contracts with six members, and the independent ability of the authority and its members to raise electric rates. The revenue defensibility assessment reflects a midrange purchaser credit quality influenced by the generally stronger financial profiles and weaker service area characteristics of ARPA members.

ARPA's operating risk and operating cost burden are low, reflecting economic purchased power costs and consistent cost management. ARPA recently signed a new fixed-price power supply contract (PSC) effective in 2025 with Guzman Energy, LLC. Given its existing and future PSCs and its long-term federal hydropower contracts, ARPA's power supply is adequate for member requirements through the 2043 life of its bond indebtedness.

ARPA reduced base energy rates by 3.5% during 2021 through savings on the retirement of its 2010 bonds, consistent with its board's directive to lower member rates. Fitch Ratings expects the authority to achieve stable leverage averaging more than 10.0x over the next three years in its base case and stress case scenarios.

Key Rating Drivers

Revenue Defensibility: 'a'; All-Requirements Wholesale Provider: The assessment reflects midrange purchaser credit quality, indicated by a purchaser credit index (PCI) of 2.5 based on ARPA's six members' credit characteristics. However, the revenue defensibility of 'a' is supported by ARPA's unconditional, all-requirements contracts that extend for the life of ARPA's outstanding debt through 2043. Rate flexibility is very strong as ARPA and its members have the legal ability to independently set rates.

Operating Risk: 'a'; Low Operating Cost Burden: Operating risk is characterized by a low operating cost burden, reflecting the authority's low purchased power costs. Power supply is provided primarily through a purchase contract with Public Service Company of Colorado (PSCo, A–/Stable) that extends to Jan. 31, 2025. Life-cycle investment needs are elevated based on a Fitch-estimated 18-year average age of ARPA's plant assets. Operating cost flexibility is neutral.

Financial Profile: 'bbb'; Elevated Leverage from Failed Lamar Repowering Project: The 'bbb' financial profile reflects ARPA's elevated leverage of 10.9x in 2021 and the expectation that metrics will range between 8.8x to 10.8x across ARPA's base case and moderate stress case scenarios. Liquidity is neutral to the rating.

Asymmetric Additional Risk Consideration: No asymmetric additional risk considerations affected this rating determination.

FACT Tools

Ratings

Long-Term Issuer Default Rating	BBB–

Outstanding Debt

Arkansas River Power Authority Power Revenue Refunding Bonds	BBB–
Arkansas River Power Authority Power Revenue Refunding Bonds (Taxable)	BBB–

Rating Outlook

Stable

Applicable Criteria

Public Sector, Revenue-Supported Entities Rating Criteria (September 2021)

U.S. Public Power Rating Criteria (April 2021)

Related Research

Public Power - Fitch Analytical Comparative Tool (FACT) - 2022 (June 2022)

U.S. Public Power -- Peer Review (June 2022)

Fitch Ratings 2022 Outlook: U.S. Public Power and Electric Cooperatives (December 2021)

Analysts

Rebecca Meyer, CFA, CPA, CISA
+1 512 215-3733
rebecca.meyer@fitchratings.com

Andrew DeStefano
+1 212 908-0284
andrew.destefano@fitchratings.com

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- ARPA maintaining Fitch-calculated leverage consistently below 10.0x in Fitch's base and stress cases;
- Sustained improvement of ARPA members' PCI consistently below 2.5x and improvement in the purchaser credit quality assessment to 'a'.

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

- Sustained deterioration of ARPA members' PCI, which could be driven by their declining service area characteristics;
- Financial performance resulting in a leverage increase to more than 12.0x on a sustained basis in Fitch's base and stress cases.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
BBB–	Affirmed	Stable	8/9/22
BBB–	Assigned	Stable	5/24/18

IDR – Issuer Default Rating.
Source: Fitch Ratings.

Credit Profile

ARPA was formed in 1979 to provide all-requirements wholesale power to its member communities in Southeast Colorado: Trinidad, La Junta, Lamar, Las Animas, Springfield and Holly. The authority's power supply is sourced from federal hydropower, renewable energy and supplemental power purchases that replaced the Lamar Repowering Project (LRP) output.

Lamar Repowering Project

The LRP was a joint effort by the authority, the Lamar Utilities Board (LUB) and the city of Lamar to repower LUB's 25MW natural gas generating unit into a 38.5MW coal-fired unit. In September 2014, the three entities decided to decommission and salvage the LRP because the project failed to meet its original objectives.

ARPA undertook steps to stabilize its finances, operations and member relationships following the project closure decision. However, the LRP left ARPA with reduced financial flexibility and strained member relationships. The authority spent approximately $174.1 million on the project, debt financing approximately $156.8 million of that total. The corresponding debt service on a nonfunctioning asset heightened ARPA's leverage, reducing its financial flexibility and resulting in higher member rates.

Three of ARPA's members filed suit in 2014 to terminate their contractual relationship with ARPA. One of the three members — Raton, NM — left ARPA, while the other two (Lamar and Trinidad) remain, having resolved their differences through settlement agreements. The settlement with Lamar totals $350,000 per year through 2043.

ARPA demolished a portion of the Lamar plant during 2020 and provided the city of Lamar with funds to enable its work with a private enterprise to repurpose the north side of plant facilities to agricultural processing from coal handling. These actions represent ARPA's final LRP operating responsibilities.

Revenue Defensibility

ARPA is an all-requirements, wholesale energy and power provider to six small municipalities located in Colorado. Members are obligated to purchase all their energy needs from ARPA pursuant to take-and-pay contracts that extend through the life of ARPA's outstanding debt.

Rate Flexibility

Rate flexibility is very strong. ARPA and its membership have the independent legal ability to raise rates without external approval. Under the terms of the power supply agreement (PSA), ARPA is able to charge its members at the rates established by its board. The board is required under the PSA to review ARPA's rates at least once a year. However, it can elect to do so more frequently to ensure rates are sufficient to cover certain defined items, including but not limited to O&M expenses, ARPA's debt service, the costs of purchased power and energy, and building reasonable reserves.

Rate changes can be made at any time with board approval, but members shall receive 30 days of notice of any rate changes unless ARPA has good cause to reduce the notice period. Under the PSA, members agree to pay ARPA's rates as operating costs of their respective electric systems. ARPA members likewise retain the independent ability to raise rates.

Purchaser Credit Quality

A 2.5x PCI indicates midrange purchaser credit quality and reflects stronger member financial profiles, but a preponderance of weaker service area characteristics and above average electric rates. The PCI factors in all six Colorado-based members: Lamar Light and Power (32%), The Electric Department of La Junta (30%), City of Trinidad Electric Utility (20%), Las Animas Municipal Utilities (10%), Town of Holly Utilities (4%) and Springfield Utility Company (4%).

ARPA does not expect significant growth among its membership, with the exception of Trinidad, a main north-south Colorado thoroughfare close to I-25. The majority of members do not have outstanding debt and liquidity is generally adequate. Rate affordability is split between midrange and weaker, which does not yet reflect ARPA's 3.6% reduction of its basic energy rate effective January 2021.

Operating Risk

ARPA consistently maintains an operating cost burden below 10 cents/kWh, averaging 6.6 cents/kWh over the past five years, and considered low by Fitch for wholesale power systems. The authority's cost burden is driven primarily by its low purchased power costs, but does not include and fully reflect the full costs of ongoing debt service associated with the LRP.

Operating Cost Flexibility

ARPA executed a long-term, fixed-price, full-service PSC with Guzman effective Feb. 1, 2025 through Oct. 1, 2043. The Guzman PSC replaces ARPA's expiring contract with PSCo. The authority expects the new contract to provide lower rates to ARPA members once the agreement is fully implemented. The contract also allows ARPA to self-supply additional renewable generation resources toward Colorado's goal of reducing greenhouse gases (GHGs).

The authority received 63% of its energy from the PSCo contract in 2021, 29% from Western Area Power Administration (WAPA) hydro power and 8% from wind. ARPA's hydro power supply is provided from two long-term hydropower contracts with WAPA, which is undergoing an approximately 35% shortfall due to the western drought. ARPA is able to backfill this energy through PSCo at this time. The authority's renewable power is provided from wind turbines owned by ARPA and its members, including the Lamar wind project.

ARPA is reviewing renewable purchased power agreement options. These include repowering the Lamar wind turbines and a federally funded solar installation. ARPA members are preparing for customer solar installations. Colorado's legislature established a goal during the 2019 session to achieve a 26% reduction in GHG emissions within the state by 2025 and 50% by 2030. The legislature also established a long-term goal of reducing GHG by 90% by 2050. However, ARPA is not required to comply with the Colorado renewable mandate based on its size and municipal utility status.

ARPA operates within the Western Electricity Coordinating Council (WECC), one of six U.S. regional entities responsible for overseeing and monitoring reliability and assessments. While power supply capacity is diverse across WECC, resource diversity varies by state. Colorado's resource mix is in flux, migrating from coal toward the GHG emission standards.

Capital Planning and Management

Lifecycle investment needs are elevated based on Fitch's estimated 18-year age of ARPA's assets as of Dec. 31, 2021. Fitch expects the average age of the authority's plant to increase further over the next five years based on ARPA's capital spending plans falling short of depreciation. ARPA's five-year capital plan of approximately $660,000 is modest and consistent with its primary reliance on purchased power and third-party transmission.

Financial Profile

ARPA's 2021 leverage remained relatively stable at 10.9x compared with 11.3x in 2017. The modest decline reflects the authority's healthy financial performance and its 2018 debt extension and restructuring. ARPA's liquidity profile is neutral to the rating. ARPA completed fiscal 2021 with 1.2x coverage of full obligations and 98 days cash on hand. ARPA's $1.5 million line of credit provided a liquidity cushion of 129 days.

Fitch Analytical Stress Test (FAST) — Base and Stress Case

Fitch's forward-looking analysis expects ARPA to maintain a stable financial profile through the base case scenario and a moderate stress case that considers the impact of reduced demand. Fitch's base case assumptions largely reflect the ARPA financial forecast, which Fitch considers reasonable. The base case indicates leverage will vary around 10.0x, peaking at 10.4x in 2024 before moderating below 9.0x.

Fitch's stress case scenario applies a reduction of sales in the first and second years of the forward-looking analysis, followed by recovery in the latter three years. The stress scenario indicates ARPA's leverage ratio would similarly vary, peaking at 10.8x in 2023 before recovering to just above 9.0x in 2026.

Debt Profile

Fitch considers ARPA's debt profile to be neutral to the rating based on its fixed-rate structure. The authority had approximately $110.7 million in series 2018 fixed-rate revenue bonds outstanding as of Dec. 31, 2021. ARPA retired its series 2010 bonds — which had $14.8 million outstanding — in January 2021. The series 2018 bonds were issued to fund LRP costs and will amortize through 2043.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Financial Summary — Arkansas River Power Authority, Colorado

($000, Audited Fiscal Years Ended Dec. 31)	2017	2018	2019	2020	2021
Net Adjusted Debt to Adjusted FADS (x)	**11.34**	**9.78**	**10.13**	**10.20**	**10.89**
Net Adjusted Debt Calculation					
Total Current Maturities of Long-Term Debt	2,375	2,840	2,950	1,015	2,835
Total Long-Term Debt	146,505	142,273	138,868	137,397	117,348
Total Debt	**148,880**	**145,113**	**141,818**	**138,412**	**120,183**
+ Capitalized Fixed Charge — Purchased Power and Gas	38,140	39,655	41,185	40,771	40,794
– Total Unrestricted Cash	6,292	11,823	16,002	17,894	4,874
Net Adjusted Debt	**180,728**	**172,946**	**167,000**	**161,289**	**156,103**
Adjusted FADS for Leverage Calculation					
Total Operating Revenue	31,171	32,194	31,204	31,095	29,430
Total Operating Expenses	17,825	17,719	18,249	18,509	18,378
Operating Income	**13,345**	**14,475**	**12,955**	**12,586**	**11,052**
+ D&A	267	266	270	269	272
+ Interest Income	118	258	500	251	9
FADS	**13,730**	**14,999**	**13,725**	**13,105**	**11,334**
+ Adjustment for Purchased Power	4,768	4,957	5,148	5,096	5,099
– Total Transfers/Distributions	2,556	2,281	2,381	2,384	2,095
Adjusted FADS for Leverage	**15,942**	**17,675**	**16,492**	**15,818**	**14,338**
Coverage of Full Obligations (x)	1.06	1.16	1.11	1.07	1.18
FADS	13,730	14,999	13,725	13,105	11,334
+ Adjustment for Purchased Power	4,768	4,957	5,148	5,096	5,099
– Total Transfers/Distributions	2,556	2,281	2,381	2,384	2,095
Adjusted FADS for Coverage	**15,942**	**17,675**	**16,492**	**15,818**	**14,338**
Full Obligations Calculation					
Cash Interest Paid	7,957	7,955	6,890	6,804	6,032
Prior-Year Current Maturities	2,260	2,375	2,840	2,950	1,015
Total Annual Debt Service	**10,217**	**10,330**	**9,730**	**9,754**	**7,047**
+ Adjustment for Purchased Power	4,768	4,957	5,148	5,096	5,099
Total Fixed Obligations	**14,984**	**15,287**	**14,878**	**14,850**	**12,147**
Liquidity Cushion (Days)	162	279	355	388	129
Unrestricted Cash (Days)	131	247	325	358	98
Liquidity Calculation					
+ Total Unrestricted Cash	6,292	11,823	16,002	17,894	4,874
+ Total Borrowing Capacity	1,500	1,500	1,500	1,500	1,500
Total Liquidity	**7,792**	**13,323**	**17,502**	**19,394**	**6,374**
Cash Operating Expense Calculation					
Total Operating Expense	17,825	17,719	18,249	18,509	18,378
– D&A	267	266	270	269	272
Cash Operating Expenses	**17,559**	**17,453**	**17,980**	**18,240**	**18,106**

FADS – Funds available for debt service. D&A – Depreciation and amortization.
Source: Fitch Ratings; Fitch Solutions; Lumesis; EIA; Arkansas River Power Authority, Colorado.

Key Definitions

Terms	Definition	Significance
Issuer Default Rating (IDR)	An expression of overall enterprise risk and relative vulnerability to default.	Provides an opinion of the relative ability of an entity to meet financial commitments, expressed as an ordinal measure of credit risk.
Standalone Credit Profile (SCP)	An expression of overall enterprise risk.	Provides an opinion of the credit quality of an entity on a standalone basis, irrespective of its relationship with, or the credit quality of, its related municipality.
Net Adjusted Debt	Adjusted debt – unrestricted cash – funds restricted for debt service	Provides an inclusive evaluation of long-term liabilities offset by funds available for debt service.
Adjusted FADS	EBITDA + interest income + 30% of purchase power expense + operating lease expense – transfers/distributions + pension expense	Provides an indication of cash flow available for the payment of debt service, adjusting for purchased power, operating lease and pension obligations.
Net Adjusted Debt to FADS	Net adjusted debt/adjusted FADS	Provides an indication of net total leverage position against available operating cash flow.
Full Obligations	Cash interest paid + scheduled long-term principal payments + 30% of purchase power expense	Provides an indication of inclusive fixed and debt service obligations.
Coverage of Full Obligations	(EBITDA + interest income + 30% of purchase power expense + operating lease expense – transfers/distributions)/full obligations	Provides an indication of the relative cushion of operating cash flow to fixed charges.
Base Case	The expected forward-looking case in the current macroeconomic environment.	Provides the analytical starting point in the forward-looking analysis, and also informs the stress case.
Stress Case	The potential performance under a common set of assumptions.	Illustrates how cycles affect individual issuers differently, and informs the level of rating stability and credit resiliency.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

DISCLAIMER & DISCLOSURES

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers. Please read these limitations and disclaimers by following this link: https://www.fitchratings.com/understandingcreditratings. In addition, the following https://www.fitchratings.com/rating-definitions-document details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default. Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct section of this site. Directors and shareholders' relevant interests are available at https://www.fitchratings.com/site/regulatory. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third- party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see https://www.fitchratings.com/site/regulatory), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.