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Connecticut Natural Gas Ratings Placed On CreditWatch Negative; Southern Connecticut Gas Co. Outlook Revised To Negative

- On Oct. 4, 2024, Connecticut's utility regulator, the Connecticut Public Utilities Regulatory Authority (PURA) published its draft decision on Connecticut Natural Gas Corp.'s (CNG) and Southern Connecticut Gas Co.'s (SCG) rate cases, where it recommended material base rate decreases for both utilities.
- Though the final order is still pending and could result in better rate outcomes, we believe the utilities' financial measures are likely to weaken significantly from current levels.
- Therefore, we placed our ratings on CNG, including our 'A' issuer credit rating on CreditWatch with negative implications. This indicates that we could lower our ratings on CNG by one notch, pending PURA's final order.
- At the same time, we revised our outlook on SCG to negative from developing. This reflects that we no longer expect SCG to attain financial measures that would lead to a higher rating. The negative outlook also reflects our view that we could lower our assessment of Connecticut's regulatory construct.

TORONTO (S&P Global Ratings) Oct. 24, 2024—S&P Global Ratings today took the rating actions listed above.

PURA's draft rate case decisions suggest a material base rate decrease for CNG and SCG.

PURA published its draft decision for both utilities rate cases. It includes material base rate decreases of about $38.8 million for CNG and about $36.6 million for SCG. While there is a possibility of better rate outcomes in the final order, the preliminary order was sufficiently negative as to indicate that there is a higher likelihood that the financial measures of both utilities will weaken significantly. We expect a final order on Nov. 18, 2024. The main elements of the draft order are:

— A reduction to rate base, because PURA allowed investments up to 2022 with some pro forma adjustments, as opposed to the utilities filing rate cases on future test years.

— A reduction to CNG's depreciation expense due to rejection of how the utility calculates salvage values.

— CNG to implement an $8 million annual credit to ratepayers over three years as a result of surplus revenues from gas sales and hardship revenues.

— SCG to implement a $29 million annual credit to ratepayers over three years reflecting refunds of regulatory liabilities associated with the Tax Cuts and Jobs Act (TCJA) of 2017.

— The continuation of the Distribution Integrity Management Program (DIMP) rider for both utilities.

CNG's funds from operations (FFO) to debt will most likely fall below 25%.

The current base rate decrease in the draft order would result in a large downward trend for CNG, where we expect FFO to debt will be 16%-18% in 2025 and 2026 compared to the company's current financial measures that have been consistently above our downgrade threshold of 25%. This would not be consistent with our current ratings on CNG.

The recommended base rate decrease would limit upside for SCG's ratings.

Our previous developing outlook on SCG reflected our expectation that its stand-alone financial performance could continue to improve, primarily due to consistent application of capital tracker mechanisms and generally consistent capital spending, leading to higher ratings. However, based on the preliminary PURA order we no longer believe that the company could attain funds from operations to debt above our upgrade threshold of FFO to debt of 25% given the increasing likelihood of material base rate decrease.

We continue to monitor Connecticut's regulatory environment.

We believe the signing of Senate Bill 7 into law is negative for credit quality because it discontinued the use of the electric system improvement charge in future rate proceedings and allows PURA to have discretion regarding the consistent implementation of decoupling. We believe these developments decrease cash flow predictability. While we believe CNG's and SCG's rate cases had issues specific to these utilities, most rate orders in Connecticut over the past 18 months significantly deviated from our base case. In general, we expect utilities in regulatory jurisdictions that are supportive of credit quality to fully recover all operating and capital costs and to operate under a consistent framework that demonstrates regulatory and cash flow stability. Accordingly, we expect to continue to closely monitor further regulatory developments, including PURA's future rate case orders and how the performance-based regulatory framework will be implemented.

- CNG

We aim to resolve the CreditWatch within the next 60 days once the final order is published by PURA, which could potentially weaken financial measures, resulting in a downgrade.

- SCG

The negative outlook reflects that we could downgrade SCG over the next 12-18 months pending our review of Connecticut's regulatory jurisdiction. Under the current draft order, we assume the company's stand-alone funds from operations (FFO) to debt will be 23%-25% in 2024 and 18%-21% in 2025 and 2026.

We could lower our ratings on SCG over the next 12-18 months if we revise downward our assessment of Connecticut's regulatory jurisdiction or SCG's ability to manage regulatory risk is diminished relative to peers We could also lower our ratings on the company if we maintain our current assessment of Connecticut's regulatory jurisdiction and its stand-alone FFO to debt weakens consistently below 16%. We could also lower the ratings if the final order is materially worse than the draft order.

We could affirm our ratings on SCG and revise our outlook to stable over the next 12-18 months if we maintain our current assessment of Connecticut's regulatory jurisdiction and SCG's stand-alone FFO to debt remains consistently above 16%.

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.

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