

RATING ACTION COMMENTARY

Fitch Rates Los Angeles, CA's Water Rev Bonds 'AA-'; Outlook Revised to Stable

Thu 23 Oct, 2025 - 1:06 PM ET

Fitch Ratings - Austin - 23 Oct 2025: Fitch Ratings has assigned a 'AA-' rating on the following water system revenue bonds issued by the Los Angeles Department of Water and Power, CA (LADWP or the department):

--Approximately \$1.03 billion water system revenue bonds series 2025C.

The bonds are expected to price on or around November 6. The proceeds will be used to refund all or a portion of the department's outstanding water system revenue bonds 2016 series A and/or 2016 series B, pay the costs of capital improvements to the department's water system (the system), and pay costs of issuance.

Fitch has also affirmed the rating on the following obligations at 'AA-':

--Approximately \$5.05 billion water system revenue bonds (pre-refunding).

Fitch has assessed the system's Standalone Credit Profile (SCP) at 'aa-'. The SCP represents the credit profile of the system on a standalone basis irrespective of its relationship with, and the credit quality of, the city of Los Angeles (the city; Issuer Default Rating [IDR] AA+/Negative).

The Rating Outlook has been revised to Stable from Negative.

RATING ACTIONS

ENTITY / DEBT ⚡

RATING ⚡

PRIOR ⚡

Los Angeles Department
of Water & Power (CA)
[Water]

| | | | | |
|--|----|---------------------------|----------|-----------------------------------|
| Los Angeles Department of Water & Power (CA) /Water Revenues/1 LT | LT | AA- Rating Outlook Stable | Affirmed | AA- Rating Outlook Negative |
|--|----|---------------------------|----------|-----------------------------------|

[VIEW ADDITIONAL RATING DETAILS](#)

The Outlook revision to Stable from Negative reflects Fitch's view that the near-term likelihood of LADWP incurring a materially significant financial liability related to the Palisades wildfire has declined.

Testimony provided in a criminal complaint affidavit (the affidavit) by a credentialed special agent from the federal Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF; the lead agency investigating the Palisades fire) states the cause of the Palisades fire on Jan. 7, 2025 as a "holdover" fire from the earlier Lachman fire that was originally ignited on Jan. 1, 2025. The affidavit attributes the cause of the Lachman fire as incendiary (i.e. an intentional ignition) and rules out other alternative ignition sources, including LADWP power equipment, for both the Lachman and Palisades fires.

While the affidavit does not comment on the state or management of LADWP's water infrastructure, it states that LADWP's electrical infrastructure was not the source of ignition. This is considered a positive development for the water system given the overlapping customer base and the potential impact a liability related to ignition could have had on customers.

Uncertainty persists due to outstanding litigation. California's unique and rigid interpretation of inverse condemnation has been cited in litigation against the water system's operations. The nearby Santa Ynez reservoir was empty and awaiting repairs at the time of the Palisades fire and is noted in litigation as a contributing factor in an inability to contain the fire sooner. Precedent around similar litigation against water utilities is sparse and results in uncertainty around any potential liability LADWP, and specifically the water system, may incur. There is additional uncertainty regarding the allocation of a potential liability between LADWP and the city, which is also named in the litigation.

However, Fitch believes the litigation (and any resulting liability, should it occur) is unlikely to be resolved over Fitch's outlook horizon. Resolution of the litigation that results in a material liability to LADWP could still result in negative rating action. The credit impact of a substantial judgement or settlement owed will largely depend on additional factors to be assessed at that time, including how/if the liability is shared between LADWP and the city, decisions regarding the use of debt and/or rate action to fund the liability, and the timeline for repayment.

The 'AA-' rating continues to reflect the system's 'Very Strong' financial profile within the framework of 'Very Strong' revenue defensibility and 'Very Strong' operating risk profile, both assessed at 'aa'. The system's leverage, measured as net adjusted debt to adjusted funds available for debt service (FADS), was very low, at 6.9x, in fiscal 2024 and is down from a high of 10.1x in fiscal 2019. In upcoming years, Fitch expects leverage to typically range between 8.5x and 9.0x in Fitch's Analytical Stress Test (FAST) rating case (assuming no wildfire liability, as discussed above), which retains a modest amount of headroom at the current rating.

The system's revenue defensibility is anchored in a rate structure that decouples demand from revenue generation and a large and diverse retail customer base in the service territory of the city of Los Angeles. Stability in the 'aa' revenue defensibility assessment is largely dependent on implementation of the automatic pass-through adjustments and recovery of targeted base rate revenue as allowed under the system's dynamic rate structure, which the system has continued to adjust in recent years even as the last rate package ended June 30, 2020.

The cost of the direct physical damage to LADWP's water facilities from the Palisades fire is manageable, at an estimated \$15 million (and an additional \$8 million in damage attributed to the concurrent windstorms), and not expected to impact the system's financial performance.

The system's 'Very Strong' operating risk profile reflects a low, albeit increasing, operating cost burden, stable life cycle ratio and healthy levels of capex. With the system's continued focus on conservation and expanding the local water supply, specifically reuse, Fitch considers the system's investment in these long-term projects a key attribute when assessing the operating risk profile.

SECURITY

The bonds are special obligations of LADWP payable solely from the Water Revenue Fund.

KEY RATING DRIVERS

Revenue Defensibility - 'aa'

Favorable Service Area, Dynamic Rate Structure

The city retains the legal authority to adjust rates as needed without external oversight, which supports revenue defensibility. The system is able to maintain solid financial performance amid generally declining demand primarily due to its unique rate structure that includes multiple automatic pass-through adjustments to recoup costs. A base rate revenue target decouples revenue generation from demand and should recover any revenue shortfall relative to the target in the following year, limiting the potential for a significant decline in FADS. Conversely, any overage is returned to customers, thereby also limiting any significant increases in FADS.

The adjusters recoup costs associated with purchased water, operations and maintenance, infrastructure costs (such as projected capital spending) and bad debt and legal expenses, among other items. A base rate revenue target is established as part of the annual budget process. Any shortfall in the revenue target would be expected to be recouped in the subsequent year's proposed base rate revenue target adjustment. A failure to implement the pass-through adjustments or adjust base rate revenue targets would likely pressure the revenue defensibility assessment as well as the rating.

Fitch considers the monthly residential water bill affordable for approximately 67% of the service area population, based on standard monthly usage of 7,500 gallons. However, rates continue to be competitive compared with other large providers in the state, and much of the pass-through adjustments affect higher-usage customers, thereby mitigating some of the effect on economically vulnerable customers.

The favorable service area is characterized by average income levels and midrange customer growth. Despite a weaker unemployment rate relative to the nation, Fitch considers the city's importance as a regional economic center when assessing the service area. Customer growth registered a five-year compound annual growth rate (CAGR) of 0.3% as of fiscal 2024. Income levels were about 2% above the national median as of 2023. The unemployment rate has decreased to 6.0% since 2020 but was still 50% more than the national average in 2024.

Operating Risk - 'aa'

Low Operating Cost Burden, Moderate Investment Needs

The system's fiscal 2024 operating cost burden was low, at \$8,407 per million gallons (mg), and its life cycle ratio was very low and favorable, at 27%. Together, these metrics support the operating risk assessment. Annual capital spending relative to depreciation is robust, averaging 350% over the last five fiscal years from 2020 to 2024. Planned capital spending for the next five years should generally outpace historical depreciation, supporting a continued very low life cycle ratio.

The system's fiscal 2026 through 2030 capital improvement program totals approximately \$7.7 billion, up from prior plans that were closer to \$6 billion to \$7 billion. As more local supply expansion projects move into the upcoming years of the capital plan, annual spending is expected to increase incrementally from around \$800 million in fiscal 2025 to over \$1.8 billion by fiscal 2029. Around two-thirds of the planned spending is expected to be debt-financed, with the balance largely funded on a pay-go basis.

Grant funding will also be pursued as available. The capital plan is not dictated by regulatory actions, so a level of flexibility exists in executing it. Failure to recover associated capital costs through the system's rate structure could result in inadequate FADS, driving leverage to a level that pressures the rating.

LADWP is working to increase local supply via recycled water. As part of its Pure Water Los Angeles initiative (Pure Water LA, previously known as Operation Next), the city is aiming to eventually recycle all wastewater. Three of the four city-owned wastewater plants already provide for reuse, but the largest plant, the Hyperion Water Reclamation Plant (HWRP), will require significant investment. Full realization of this initiative is expected over the next 20 to 30 years. Therefore, associated costs would be incrementally financed and are not an immediate pressure on margins.

Financial Profile - 'aa'

Leverage to Remain Generally Stable

The system's leverage measured 6.9x as of fiscal 2024. This is the lowest level in several years, benefiting from receipt of state Prop. 1 grant funding, which reimbursed the system for previously incurred capital projects and boosted FADS for the year. Absent volatility in pension valuations and expenses, leverage more typically measured between 8.0x and 9.0x since fiscal 2020. The liquidity profile is neutral to the overall assessment, with coverage of

full obligations (COFO) of 1.9x. Fitch-calculated total debt service coverage was 2.0x in fiscal 2024, which excludes fixed service expense.

The liquidity cushion of 314 days in fiscal 2024 reflects additional liquidity provided by a \$300 million revolving credit agreement (RCA) that can be drawn upon by either LADWP's water system or its power system. The RCA was subsequently increased to \$500 million in July 2025. As of Oct. 1, 2025 the department had \$300 million outstanding under the RCA payable from the water fund.

The FAST considers the potential trend of key ratios in a base case and stress scenario over a five-year period. The stress scenario is designed to impose capital costs 10% above expected base case levels and evaluate potential variability in projected key ratios. The FAST reflects Fitch's view of a reasonable scenario, which is generally informed by publicly available and/or management provided information with respect to capex, user charges and rate of revenue and expenditure growth.

Given the annual cost adjustment within the system's rate structure meant to recover capital spending, Fitch would expect any increase in unplanned capital spending to be recovered in the subsequent year as additional operating revenue. As such, the base case is considered the rating case, as the stress case reflects additional FADS recovery and drives slightly lower leverage results. The rating case reflects leverage that ranges between 8.5x and 9.0x in most years. The liquidity profile is expected to remain neutral to the assessment over the five-year horizon.

The risk of a large wildfire judgement or settlement from the litigation could impact the system's financial profile. While the current rating includes some headroom for additional debt above current planned levels, the magnitude of damages from the Palisades wildfire could outpace headroom at the current rating. The Stable Outlook is reflective of Fitch's view that a determination of any potential legal liability is likely beyond our Rating Outlook horizon.

Asymmetric Additional Risk Considerations

No asymmetric additive risk considerations affected this rating determination.

RATING SENSITIVITIES

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

--Potential of wildfire-related liability that results in long-term dilution of LADWP's financial profile, which potentially has a multi-notch impact;

--Sustained actual and projected leverage over 10.0x in Fitch's rating case, assuming stability in the revenue defensibility and operating risk assessments;

--A downgrade of the city's IDR to below 'AA-';

--Local political action to forego the next multi-year rate case, which weakens LADWP's financial profile.

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

--Positive rating action is unlikely without greater clarity around the outcome of pending litigation and any resulting liability potentially incurred as a result of the Palisades fire;

--Actual and projected leverage below 9.0x on a sustained basis in Fitch's rating case, assuming stability in the revenue defensibility and operating risk assessments.

PROFILE

The city is the commercial and cultural center of a very large, diverse economy. LADWP provides retail water service to nearly 700,000 customers serving an estimated population of 3.8 million. The service area mostly overlaps with the city limits, covering about 470 square miles. LADWP's water supply is derived from four sources: 1) deliveries via the city's Los Angeles Aqueduct (LAA); 2) local groundwater; 3) recycled water; and 4) imported water purchased from Metropolitan Water District of Southern California (MWD; IDR AA+/Stable), which typically provides the remaining water supply not available from the first three sources and is typically the highest cost supply.

Deliveries from the LAA, which are the least costly supply, increased in the second half of fiscal 2023 after a very wet winter, and remained high through fiscal 2024 given sound hydrological conditions. Through the third quarter of fiscal 2025, nearly half of the supply was delivered via the LAA.

The system owns and operates an extensive distribution, storage and treatment system. As noted, supply is diverse, and adequate for the foreseeable future, yet continued work to expand the local supply remains a focus of the capital program. The various treatment facilities provide sufficient capacity that material expansion is not a focus of the capital plan.

Fitch considers the system to be a related entity to the city for rating purposes given the city's oversight of the system, including the authority to establish rates and the city's reporting of the department as an enterprise fund of the city. The credit quality of the city does not currently constrain the bond rating. However, because the bonds do not have a secured lien on water system revenues, the bond rating is capped by the city's IDR pursuant to Fitch criteria.

Updated U.S. Environmental Protection Agency (EPA) Regulations

The EPA's enhanced focus on lead and copper lines and per- and polyfluoroalkyl substances (PFAS) contaminants has led to the finalized Lead and Copper Rule Improvements (LCRI) along with specific testing requirements for PFAS. The system completed the required service line inventory and no lead service lines were identified, but expects the testing requirements at schools in the service area will require significant effort.

The system regularly tests for PFAS. PFAS have been detected in individual wells, but water from individual wells is blended with large volumes of surface water and other sources before entering the distribution system, resulting in results below maximum contamination limits.

Sources of Information

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by data from DIVER by Solve.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The ESG Relevance Score for Exposure to Environmental Impacts is changed to '3' from '4' due to the noted investigative findings regarding the Palisades fire ignition.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more

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APPLICABLE CRITERIA

[U.S. Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 10 Jan 2025\) \(including rating assumption sensitivity\)](#)

[U.S. Water and Sewer Rating Criteria - Effective from February 2025 to February 2026 \(pub. 24 Feb 2025\) \(including rating assumption sensitivity\)](#)

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Los Angeles Department of Water & Power (CA)

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