FitchRatings

Fitch Affirms Dominion Resources & Subs; Dominion Gas Holdings' Outlook Revised to Negative

Fitch Ratings-New York-03 May 2017: Fitch Ratings has affirmed the 'BBB+' Issuer Default Rating (IDR) of Dominion Resources, Inc. (DRI) and the 'A-' IDRs of DRI subsidiaries Virginia Electric and Power Co. (VEPCo), Dominion Gas Holdings, LLC (DGH), and Questar Gas Company (Questar). Fitch has also affirmed the companies' debt instrument ratings as listed at the end of this release. The Rating Outlook for DRI, VEPCo, and Questar is Stable. The Rating Outlook for DGH has been revised to Negative from Stable.

The Negative Outlook for DGH reflects leverage that remained elevated at the end of 2016 as a result of management's previous strategy to move debt from corporate parent DRI to DGH to achieve a more balanced capital structure at the parent level. As a result, higher debt levels and recent variability in DGH's cash flows have resulted in leverage measures that are high for the rating level. For the year ended Dec. 31, 2016, DGH adjusted debt/EBITDAR of 4.8 is materially above Fitch's previously stated rating sensitivity of 3.75x. FFO adjusted leverage for the same period is 5.7x versus prior sensitivity of 4.25x. While Fitch expects some organic improvement in DGH's metrics, DRI may need to adjust financial policies to keep DGH's credit measures commensurate with the current ratings.

KEY RATING DRIVERS FOR DRI

Diversified Asset Base: DRI owns a large portfolio of utility, power, midstream and other energy assets that provides a diversified and stable source of earnings and cash flow. DRI's financial strength is currently anchored by VEPCO, a large integrated electric utility. However, VEPCOs percentage of DRI's earnings and cash flow will decrease over time due to DRI's significantly expanding gas infrastructure business.

Large Capex Plan: Fitch expects DRI's business risk profile to be elevated for the next few years, reflecting the construction risks associated with various large-scale projects, including the Cove Point liquefied natural gas (LNG) export facility, which is expected to enter service in late 2017. Timely execution of major projects are important drivers for the expected parent-level debt reduction, given expected cash flow and in some cases, asset sale proceeds from drops to affiliated master limited partnership (MLP).

Parent-Level Debt: The percentage of DRI parent-level debt is high, reflecting the prior centralized funding strategy for all subsidiaries and operations except VEPCo, DGH, and the recently acquired Questar. DRI level debt currently accounts for approximately 50% of consolidated indebtedness. While there are significant cash flows generated by the DRI-directly held assets, large capital projects have resulted in elevated leverage on a both a consolidated and deconsolidated basis. Fitch expects management to adhere to stated goal of reducing DRI level debt to 30%-40% of total indebtedness by 2020.

Financial Profile: Consolidated leverage is high for the rating level but should gradually improve over the next several years as DRI realizes anticipated earnings contributions from projects currently under construction and expected sizeable asset drops to its MLP. Fitch expects that DRI consolidated 2016 debt/EBITDAR of 6.3x will improve dramatically as assets become operational. As such, consolidated leverage will likely fall to 4.6x by the end of the forecast period and funds flow from operations (FFO) leverage return to just below 5.0x from the current 6.4x.

Cash Flow Subordination: The creation of DM and subsequent IPO in 2014 provided DRI another vehicle to raise capital and monetize existing assets and investments. The MLP structure offers greater tax efficiency since earnings are not subject to corporate taxation and potentially a lower cost of capital. With its general partner interest, DRI participates in growth at the MLP through incentive distribution rights. DRI owns 100% of the general partner interest and 51% of the limited partnership units (of Dec. 31, 2016). While asset drops to DM is expected to be the key driver to DRI-level debt reduction, it adds a level of cash flow subordination and corporate complexity.

KEY RATING DRIVERS FOR VEPCo

Strong Credit Profile
VEPCo's current and projected credit metrics are supportive of the ratings. Fitch forecasts adjusted debt/EBITDAR to approximate 3.4x over the next few years, funds flow from operations (FFO) lease-adjusted leverage 3.5x, and FFO fixed-charge coverage to remain above 6.0x. By comparison, these figures were 3.1x, 3.3x and 6.4x, respectively, for the latest 12 months (LTM) ended Dec. 31, 2016.

Constructive Regulatory Environment
Fitch considers the regulatory environment in Virginia and North Carolina to be constructive, due largely to rider mechanisms that provide timely cost recovery of invested capital, including incentive returns on certain generation projects. In Virginia, VEPCo's primary regulatory jurisdiction, adjustment clauses are in place to recover costs for new generation projects, FERC-approved transmission costs, environmental compliance, energy efficiency and renewable energy programs.

Large Capex Plan
Capex is expected to remain elevated over the forecast period. The timely cost recovery mechanisms available to VEPCo soften the financial strain of funding the capex plan. Capex (including nuclear fuel) aggregates $8.5 billion over 2017-2019, including a peak of $2.9 billion in 2018, compared with $8.7 billion over the prior three year forecast. Approximately two-thirds of the capex is growth-related and the remainder is maintenance. Fitch's forecast assumes timely execution of the capital plan and that funding will be managed to maintain a balanced capital structure.

Biennial Review Suspension
Legislation enacted in Virginia in February 2015 suspends biennial reviews after 2015 until 2022 and freezes base rates through 2019. Fitch considers the impact to be credit neutral. During the rate-freeze period rider mechanisms remain in place and VEPCo can retain any earnings in excess of its authorized return on equity of 10%. VEPCo is at risk for unexpected storm costs and increased operating and capital costs not subject to rider mechanisms. The 2022 biennial review will address rates in 2020 and 2021.

Favorable Service Territory Demographics
A large government and military presence tends to limit economic and sales volatility. In addition, VEPCo's service territory has experienced strong growth of data centers due in large measure to its proximity to Washington, D.C. and high-capacity fiber networks. The service area also benefits from an attractive climate and sound economy that drives residential customer growth.

KEY RATING DRIVERS FOR DGH

Stable and Diverse Operations: The majority of DGH's earnings and cash flow comes from pipeline subsidiary Dominion Transmission and LDC Dominion East Ohio. DGH's transmission and distribution entities benefit from long-term transportation contracts, strategic location and supportive federal and state regulation. Other DGH businesses with a somewhat higher risk profile are the storage, gathering and processing of natural gas and the sale of natural gas liquids (NGL). Commodity price risk from NGL sales and recontracting, volumetric and counterparty risk are primary credit concerns.

Well-Situated Assets: DGH's assets are well positioned to benefit from the significant supply growth in the Marcellus and Utica shale basins. The supply growth is driving increased investment in new pipeline projects that earn relatively attractive Federal Energy Regulatory Commission (FERC) authorized returns. DGH also has entered into a number of farm-out transactions that generate additional revenue from lease acquisition payments and potentially long-term royalty streams.

Large Capex Plan: Fitch expects capex to remain elevated and front-end loaded over the next three years, given the large number of growth projects underway or anticipated, plus the pipeline infrastructure and replacement program at Dominion East Ohio (DEO) and maintenance capex. The investments are largely related to market access and producer outlet projects to support the expanding gas production in Marcellus and Utica. Ratings assume capex will be funded in a manner to support a balanced capital structure.

Elevated Leverage: Higher debt balances from capex spending and variability in DGH's cash flows have resulted in leverage measures that are high for the rating level. Leverage remained elevated at the end of 2016 as a result of management's previous strategy to move debt from corporate parent DRI to DGH and to achieve a more balanced capital structure at the parent level. For the year ended Dec. 31, 2016, DGH adjusted debt/EBITDAR of 4.8 is materially above Fitch's previously stated rating sensitivity of 3.75x. FFO adjusted leverage for the same period is 5.7x versus prior sensitivity of 4.25x. While Fitch expects some organic improvement in DGH's metrics, DRI may need to adjust financial policies (e.g. payment of dividends to DRI) to keep DGH's credit measures commensurate with current ratings.

Natural Gas Price Environment: Although direct commodity price exposure is limited, low prices for natural gas and NGL and associated curtailment of third-party drilling has an adverse effect on transportation volumes, on the value of NGL and consequently on DGH's earnings and cash flow. The low-price environment also has the potential to reduce future pipeline investments and anticipated earnings growth.

KEY RATING DRIVERS FOR QUESTAR

Low Risk Business Profile: Questar is a local gas distribution utility serving customers in Utah, Wyoming, and Idaho. The majority of the company's customers are located in the state of Utah, which continues to experience significant growth. Questar's customer count increased by 1.7% in 2016, and is expected to continue to increase over the forecast period in line with Utah's economic growth.

Limited Regulatory Risk: Utah has implemented numerous rider mechanisms (including weather normalization, revenue decoupling, infrastructure replacement, and purchased gas adjustment) that serve to reduce regulatory lag and stabilize credit metrics. ROEs granted in Utah are generally in line with the industry averages. As a result of the Utah and Wyoming commissions' approval of the acquisition by DRI, Questar is currently precluded from filing a base rate case in Utah before July 2019 and in Wyoming from filing a general rate case with an effective date early than January 2020.

Strong Financial Metrics: Credit measures are in-line with current rating level.

The company's numerous riders help offset potential impact from the agreed to stay out provisions. Additionally, Dominion's agreement to maintain Questar' total equity/total capitalization at a minimum of 48% (thru Dec. 2019) underpins Questar's credit quality.

Manageable Capital Expenditures: Like most gas utilities, Questar has experienced increasing capital expenditures for growth, reliability, and infrastructure upgrades. As part of the merger approval, Questar and DRI committed to spending the following capital expenditures to maintain and improve Questar' facilities: $209 million in 2017, $208 million in 2018, and $233 million in 2019. Any variances to this plan are to be supported by Questar in its next general rate case. While the elevated capital expenditures exert some pressure on Questar's credit metrics, ratios are expected to remain in line with its current rating level.

DRI Ownership: As of September 2016, Questar is an indirect subsidiary of DRI. Questar benefits from numerous ringfencing provisions in the merger approval, including separate books and records, separate legal entity, and DRI's commitment to maintain minimum 48% total equity/total capitalization at Questar thru Dec 2019. DRI also committed to using reasonable efforts to maintain credit metrics consistent with strong investment-grade credit ratings (i.e. targeting 'A' range.)

Liquidity: Questar has adequate liquidity. As a result of the acquisition by D, Questar was added as a borrower on DRI's two credit facilities which total $5.5 billion. While Questar' sublimit is set initially at $250 million it can be revised as needed. As per the Utah merger agreement, DRI has agreed that it will provide Questar with access to no less than $750 million in short-term debt or commercial paper programs.

KEY ASSUMPTIONS

Fitch's key assumptions within the rating case for DRI include:
--Growth capex will remain elevated through 2019;
--VEPCo's base rates remain frozen through 2019;
--VEPCO annual sales growth of 1% in 2017 and 1.5% thereafter;
--Maintenance of VEPCO, DGH, and Questar's capital structures inline with

regulatory capital structures (approximately 50%);
--Cove Point will enter commercial operations by the end of 2017;
--Cove Point will be fully dropped into DM by 2020, with significant amount of proceeds used to reduce DRI level debt to 30%-40% of consolidated debt.

Fitch's key assumptions within the rating case for VEPCo include:
--Base rate freeze through 2019;
--Annual sales growth of 1% in 2017 and 1.5% thereafter;
--Continuation of existing rider mechanism;
--Timely execution of capex plan.

Fitch's key assumptions within the rating case for DGH include:
--Timely execution of capital plan;
--Maintenance of a balanced capital structure;
--Reduction of leverage to levels commensurate with current ratings
--No meaningful increase in commodity exposure.

Fitch's key assumptions within the rating case for Questar include:
--Annual customer growth of 2.3%;
--Capital expenditures of $209 million in 2017, $208 million in 2018, and $233 million in 2019;
--General rate case filings in Utah and Wyoming in 2H19.

RATING SENSITIVITIES

DRI
Positive Rating Action: Positive rating action is not expected at this time given the large capital investment plan and high consolidated leverage. However, ratings could be upgraded if adjusted debt to EBITDAR falls below 3.5x and FFO lease-adjusted leverage below 4.25x on a sustainable basis.

Negative Rating Action: Ratings could be downgraded if there are substantial cost overruns or delays in completing the Cove Point LNG export project. Additionally, ratings could be downgrades if significant proceeds from asset drops to DM are not used to reduce parent level debt. Weaker earnings, lower dividends from VEPCo, or FFO-adjusted leverage above 5.0x on a sustained basis could also lead to negative rating action.

VEPCo
Positive Rating Action: A positive rating action is not expected in the near future given the large capex plan and rate freeze. However, ratings could be upgraded if Fitch were to expect adjusted debt/EBITDAR to fall below 3.3x and FFO lease-adjusted leverage below 3.5x on a sustainable basis.

Negative Rating Action: An increase in adjusted debt/EBITDAR above 3.5x and FFO-adjusted leverage above 4.3x on a sustainable basis could lead to a downgrade. While not anticipated, a significant shift in existing regulatory support in Virginia could lead to a negative rating action. A downgrade of two notches or more at DRI would also likely trigger a downgrade of VEPCo under Fitch's parent and subsidiary linkage criteria.

DGH
Positive Rating Action: Positive rating action is not expected at this time, given DGH's Negative Outlook. However, ratings could be upgraded if adjusted debt/EBITDAR falls below 3.25x and FFO lease adjusted leverage below 3.5x on a sustainable basis.

Negative Rating Action: Ratings could be downgrade if Fitch does not see improvement in expected metrics in line with our prior stated thresholds of debt/EBITDAR above 3.75x and FFO adjusted leverage above 4.25x. A downgrade of two notches or more at DRI would also likely trigger a downgrade of DGH under Fitch's parent and subsidiary linkage criteria.

Questar
Positive Rating Action: Positive rating action is not expected in the near term given Questar' current metrics and minimal geographic diversity.

Negative Rating Action: Negative rating action would be considered if Questar' adjusted Debt/EBITDAR is above 4.0x on a consistent basis. Significant credit degradation of DRI's credit quality could also result in negative rating action. A downgrade of two notches or more at DRI would also likely trigger a downgrade of Questar under Fitch's parent and subsidiary linkage criteria.

LIQUIDITY

Fitch considers DRI to have adequate liquidity. On Nov. 10, 2016, DRI, along with DRI, VEPCO, DGH, and Questar entered into a $5 billion amended and restated revolving credit agreement (core facility) and a $500 million letter of credit facility. In addition to direct borrowing, the two credit facilities support the issuance of CP. Both credit facilities mature in April 2020. As of Dec. 31, 2016, DRI has $2.3 billion of unused capacity under its credit facilities.

FULL LIST OF RATING ACTIONS

Fitch has affirmed the following ratings with a Stable Outlook:

Dominion Resources, Inc.
--Long-term IDR at 'BBB+';
--Senior unsecured debt at 'BBB+';
--Junior subordinated at 'BBB';
--Enhanced junior subordinated at 'BBB-';
--Trust preferred at 'BBB-';
--Short-term IDR at 'F2';
--Commercial paper at 'F2'.

Virginia Electric and Power Co.
--IDR at 'A-';
--Senior secured debt and revenue bonds at 'A+';
--Senior unsecured debt and revenue bonds at 'A'/'F2';
--Short-term IDR at 'F2';
--Commercial Paper at 'F2'.

Questar Gas;
--IDR at 'A-';
--Senior unsecured debt at 'A'
--Short-term IDR at 'F2';
--Commercial Paper at 'F2'.

Fitch has affirmed the following ratings:

Dominion Gas Holdings, LLC
--IDR at 'A-';
--Senior unsecured debt at 'A-';
--Short-term IDR at 'F2';
--Commercial Paper at 'F2'.

The Rating Outlook is revised to Negative from Stable.

Fitch has withdrawn the following ratings:

Consolidated Natural Gas Co. (debt assumed by Dominion Resources.)
--IDR 'BBB+'.

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Applicable Criteria
Criteria for Rating Non-Financial Corporates (pub. 10 Mar 2017) (https://www.fitchratings.com/site/re/895493)

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