

**New Issue: Moody's assigns Aaa to \$450M Massachusetts CTF bonds; outlook stable**

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Global Credit Research - 22 Oct 2015

**Aaa rating applies to \$2.0B of outstanding CTF bonds**

MASSACHUSETTS (COMMONWEALTH OF)  
State Governments (including Puerto Rico and US Territories)  
MA

**Moody's Rating**

<b>ISSUE</b>	<b>RATING</b>
Commonwealth Transportation Fund Revenue Bonds (Rail Enhancement Program) Series 2015A	Aaa
<b>Sale Amount</b>	\$450,000,000
<b>Expected Sale Date</b>	11/05/15
<b>Rating Description</b>	Special Tax: Transportation-Related

**Moody's Outlook** STA

NEW YORK, October 22, 2015 --Moody's Investors Service has assigned a Aaa rating to the Commonwealth of Massachusetts' \$450 million Commonwealth Transportation Fund (CTF) Revenue Bonds (Rail Enhancement Program) Series 2015A. We maintain Aaa ratings on the commonwealth's outstanding CTF debt, which post-sale will total \$2 billion. The bonds are scheduled to price November 5, 2015.

**SUMMARY RATING RATIONALE**

The Aaa rating reflects strong bondholder protections that include a four times additional bonds test; four times non-impairment covenant; good historical performance of the pledged revenue sources and strong coverage of maximum annual debt service. The rating also reflects the need for the pledged revenues to be appropriated annually for debt service, balanced by a mechanism that prohibits their use for any purpose unless that appropriation is made, and the segregation of the pledged revenues from general obligation bondholders.

**OUTLOOK**

The outlook for the Commonwealth of Massachusetts' Commonwealth Transportation Fund bonds is stable, reflecting the strong legal structure of the bonds and healthy debt service coverage.

**WHAT COULD MAKE THE RATING GO DOWN**

- Additional leverage or decline in the pledged revenues that materially weakens debt service coverage
- Non-appropriation of funds for debt service

**STRENGTHS**

- A strong additional bonds test that requires four times coverage of maximum annual debt service and the commonwealth's covenant not to alter the pledged revenues if it would result in maximum annual debt service coverage of less than four times
- The deposit and segregation of the pledged revenues with the bond trustee and a legal structure that provides sufficient insulation of them from the competing claims of the commonwealth's general obligation bondholders
- Strong debt service coverage provided by the pledged gas taxes and motor vehicle-related fees

## CHALLENGES

- The need for annual legislative appropriation for debt service, although that is balanced by a mechanism that prohibits the use of the pledged funds for any other purpose unless that appropriation is made and the separation of the pledged revenues from general obligation bondholders
- The aggregate limitation on debt secured by the pledged revenues is statutory and could be increased going forward

## RECENT DEVELOPMENTS

Recent developments are incorporated in the Detailed Rating Rationale.

## DETAILED RATING RATIONALE

### TAX BASE AND NATURE OF PLEDGE: CTF BONDS SECURED BY A DIVERSE STREAM OF TRANSPORTATION-RELATED TAXES AND FEES

The CTF bonds are secured by a broad mix of transportation-related taxes and fees. The bonds have a first lien pledge on 73% of the commonwealth's 24 cent fuel excise tax, collected on each gallon of gasoline (other than aviation fuel), 100% of the tax collected on special fuels and liquefied gas sold in Massachusetts, and 100% of motor carrier taxes. Massachusetts increased its gas tax from 21 cents per gallon to 24 cents effective August 1, 2013 and is moderate compared to its northeast neighbors. A provision enacted by the legislature to further adjust the gas tax annually for inflation was repealed by voters in 2014.

Additionally, the bonds are secured by a first lien pledge of a variety of motor vehicle license, registration and title fees (commonly referred to as Registrar of Motor Vehicles or "RMV" fees). RMV fees were increased in fiscal years 2003, 2009 and again in 2015. After debt service is paid on the commonwealth's outstanding 1994 Trust Indenture Special Obligation Revenue Bonds (senior and subordinate bonds both closed with final maturities in 2022). The CTF bonds also are backed by the excess of 6.86 cents of the gasoline fuels excise. Combined, fuels excise taxes account for 56.0% of the pledged revenues and motor vehicle fees are 43.2%. Additionally, the federal Build America Bond and Recovery Zone Development Bond interest subsidies received in conjunction with the 2010 issuance (which total a maximum of \$12.3 million annually) are pledged to the bonds.

### DEBT SERVICE COVERAGE AND REVENUE METRICS: PLEDGED REVENUES PROVIDE HEALTHY DEBT SERVICE COVERAGE

The CTF pledged revenues provide strong debt service coverage. Based on fiscal 2015 CTF pledged revenues of \$1.3 billion and debt service on the outstanding bonds and the current issue, coverage of maximum annual debt service (MADS) is 10.1 times. Using the same fiscal 2015 revenue and based on MADS on the full planned \$3.6 billion of CTF issuance (the outstanding and current issues, plus planned issues through 2020) coverage is a strong 6.0 times, indicating that even with higher leverage the pledged revenues can withstand another economic downturn and still maintain healthy coverage.

Historical performance of the pledged revenues is good. Consumer responses to changes in gas prices over the long term is relatively inelastic, although during fiscal 2006 the taxes and fees that are now the pledged CTF revenues declined by 4.7%, the largest decrease since fiscal 1996. During the more recent economic downturn, collections of motor fuels taxes declined by 2.8% in fiscal 2009 while RMV fees increased by 1.7%, equaling a decline in total pledged revenues of 1.1%. Since then, pledged revenues have grown annually. Strong growth of 7.8% in fiscal 2014 reflects the gas tax increase approved in 2013. For fiscal 2015, the commonwealth recorded a healthy 5.7% increase in pledged revenues, reflecting an increase in registry fees implemented on July 1, 2014.

### DEBT AND LEGAL COVENANTS: FIRST RAIL ENHANCEMENT OFFERING; BONDHOLDER PROTECTIONS INCLUDE STRONG ADDITIONAL BONDS TEST AND NONIMPAIRMENT COVENANT

CTF bonds are issued under two programs: the Accelerated Bridge Program and Rail Enhancement Program. The current issuance is the first debt offering under the Rail Enhancement Program, the issuance of which was authorized in 2014 to help finance transit and commuter rail projects throughout Massachusetts. Nearly \$1.9 billion is expected to be issued by 2020 to fund the program, including the current issuance.

The Accelerated Bridge Program has \$1.5 billion in outstanding CTF bonds, and an additional \$699.9 million Grant Anticipation Notes outstanding. The ABP was created in 2010 to fund capital improvements to bridges and related infrastructure, with total authorization of approximately \$3.0 billion in debt to fund the improvements.

The additional bonds test (ABT) requires the pledged revenues to equal four times maximum annual debt service on outstanding bonds and the planned issuance in any 12 of the prior 18 months prior to issuance. A strong non-impairment covenant allows the commonwealth to reduce the pledged revenue tax rates or base but only if that action would continue to result in at least four times coverage of maximum annual debt service. Inclusion of the BAB subsidies received as part of the 2010 issue in the pledged revenues somewhat dilutes those protections but not materially; they are still strong relative to similar credits and the ability to issue new bonds under the BAB program has expired.

#### MANAGEMENT AND GOVERNANCE: SEPARATION FROM GO CREDIT RESULTS IN ONE NOTCH RATING DISTINCTION

The CTF is one of the commonwealth's two major budgeted funds (the General Fund is the other), and makes essentially all of its transportation expenditures from it. The Massachusetts constitution limits the use of transportation-related revenues to transportation purposes, which could be interpreted broadly in certain circumstances. In our opinion, however, the CTF revenues are adequately-enough segregated from competing claims, including those of general obligation bondholders, to result in a rating one notch higher than the commonwealth's general obligation rating of Aa1/stable.

That separation is based on several factors. The authorizing statute under which the bonds are issued, the Special Obligation Act, permits the state treasurer to enter into a trust agreement and to pledge the CTF revenues and all right and title to them to bondholders, a pledge the act says is perfected. The pledged revenues are collected by the commonwealth and, as required by the trust agreement, transferred by the state treasurer to the trustee monthly (within ten days of the end of the month) for deposit into the Revenue Account. That account is subject to the pledge created by the master trust and cannot be used for any other purpose until debt service on the CTF bonds has been paid.

Immediately after receiving the monthly transfer of CTF funds from the state treasurer, the trustee is required to make a deposit into the Debt Service Fund equal to one-fifth interest and one-tenth principal. Like general obligation bonds in Massachusetts, the use of CTF funds for debt service requires annual legislative appropriation, and as long as one is made, the trust agreement permits excess CTF revenues to be released to the commonwealth for operating uses by its department of transportation (MassDOT). If no debt service appropriation is made, the trustee is prohibited from releasing any CTF revenues, precluding their use for any other purpose and giving Massachusetts strong incentive to authorize use of the funds.

#### KEY STATISTICS

- Fiscal 2015 CTF pledged revenues: \$1.3 billion
- Pro-forma coverage of maximum annual debt service: 10.1x
- Additional bonds test: 4.0 times
- Post sale CTF bonds outstanding: \$2.0 billion
- Post sale GANs outstanding: \$699.9 million
- Debt service reserve fund: n/a

#### OBLIGOR PROFILE

The Commonwealth of Massachusetts has a population of 6.7 million people and a gross state product of approximately of over \$420 billion. The state is economically well diversified and has very high wealth levels.

#### LEGAL SECURITY

The CTF Bonds are special limited obligations of the commonwealth and are payable solely from the pledged revenues, which are primarily comprised of Motor Fuel Taxes and Registry Fees.

#### USE OF PROCEEDS

Proceeds of the new bonds will be used to help finance rail improvement projects in Boston (Aaa stable), including an extension of the Massachusetts Bay Transportation Authority's (senior sales tax revenue bonds Aa2 stable) Green Line subway line, new rail cars for the Orange and Red Lines and improvements to the Fairmount rail line

and South Station passenger rail hub. Other statewide projects include the beginning phase of the South Coast rail extension project, along with the realignment of the Amtrak (A1 stable) Vermonter line and other improvements in the state's Knowledge Corridor.

#### RATING METHODOLOGY

The principal methodology used in this rating was US Public Finance Special Tax Methodology published in January 2014. Please see the Credit Policy page on [www.moody.com](http://www.moody.com) for a copy of this methodology.

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