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Summary:

Massachusetts; Federal or state grant programs

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Summary:

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Credit Profile

US\$287.865 mil fed hwy GANs (Accelerated Br Prog) ser 2013 A due 06/15/2027

Long Term Rating AAA/Stable New

Massachusetts fed hwy GANs (ASSURED GTY)

Unenhanced Rating AAA(SPUR)/Stable Affirmed

Massachusetts spl oblig

Long Term Rating AAA/Stable Affirmed

Massachusetts GANs (Accelerated Br Prog)

Long Term Rating AAA/Stable Affirmed

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services has assigned its 'AAA' rating to Massachusetts' pro forma \$288 million series 2013A federal highway grant anticipation notes (GANs). At the same time, Standard & Poor's has affirmed its 'AAA' rating on the commonwealth's GANs and special obligation notes outstanding. The outlook is stable.

Bond proceeds will continue funding repair of Massachusetts' structurally deficient bridges under its Accelerated Bridge Program, in tandem with Commonwealth Transportation Fund (CTF) bonds. The state has total authorization authority for about \$1.1 billion of GANs and \$1.88 billion of CTF bonds. The program has a scheduled completion date of September 2016, and management reports it is ahead of schedule.

The ratings reflect our opinion of the creditworthiness of the GAN program structure, which has strong debt service coverage (DSC), a subordinate backup pledge of dedicated state transportation funds, and sound bond provisions.

In 2010, Massachusetts issued new-money and refunding GANs. It issued the former under a 2010 trust agreement (2010 TA), and the refunding GANs and special obligation notes outstanding under a 1998 trust agreement (1998 TA), which is now closed. The 2013A GANs are also issued under 2010 TA.

We believe specific credit strengths include the following factors:

- In the case of the special obligation and refunding GANs, a senior position on federal highway reimbursements from the state, a closed lien, and maturity occurring in 2015;
- In the case of all GANs issued under 2010 TA, an additional pledge of excess CTF revenues under the 2010 TA -- funded from gas taxes and vehicle-registration fees -- that are pledged to CTF bonds, which Massachusetts must first pay;
- Strong maximum annual debt service (MADS) coverage of 3.01x based on budgeted 2014 federal highway reimbursements to the commonwealth of \$629 million, and very strong projected coverage of 8.48x incorporating excess CTF revenues assumed for the 2014 year. Both figures include additional GAN and CTF issuances totaling

\$1.62 billion through 2016;

- A requirement in both the 1998 and 2010 TAs that debt service payments be funded with the trustee a year in advance;
- Sound bond provisions that prohibit additional 2010 TA GAN issuances unless the commonwealth meets an effectively 4x pro forma MADS test; and
- Variable-but-generally-positive trends in obligation authority and receipts of Title 23 federal aid money, a track record of maximizing federal grants, and effective management of the grant reimbursement process.

In our opinion, credit weaknesses are similar for other grant anticipation revenue notes, including possibly lower pledged revenues resulting from a decline in funds for states from the Highway Trust Fund (HTF) or in Congressionally appropriated amounts, changes to the federal aid highway program, and delays to congressional reauthorization or the commonwealth's failure to prudently manage the reimbursement process.

The 2003A and 2010A refundings have a final maturity of 2015, and will be pre-funded a year in advance in June 2014. The 2010A new money GANs have a final maturity of 2023, with interest-only payments until 2016. We understand Massachusetts has structured debt service payments in this manner due to the 1998A TA GANs holding a senior position. However, we do not view the 2010 TA GANs' subordinate nature negatively. The 2013A GANs mature in 2027, and Massachusetts plans to issue GANs in 2014 (\$227 million) and 2015 (\$307 million) also to complete the program.

Unlike many grant-anticipation structures, both the 1998 and 2010 TAs include an additional pledge. In the case of the 1998 agreement, the pledge is both a debt service reserve (10% of MADS) and 13 cents of the state's now 24-cent gas tax (raised three cents in July), following payment of CTF bonds. However, these are accessible only in the event of a true-up condition, defined as the nationwide, Congressionally appropriated amount for highway aid from the HTF being less than \$17.1 billion in the current federal fiscal year and the GANs' DSC ratio for the next fiscal year being below 1.2x. Standard & Poor's considers either possibility unlikely and the combination to be extremely remote.

As stated, the 2010 TA has an additional backup pledge in the form of excess CTF pledged revenues, after payment of bonds backed by such revenues. The commonwealth most recently issued estimates that \$1.1 billion-\$1.2 billion in excess CTF money will be available to pay 2010 TA GANs, if necessary, which assumes an additional \$804 million in CTF bond issuances through 2016. Although the legislature can appropriate excess CTF revenues if needed, these revenues are frozen in the event they are not, and may not be used for any other purpose. Furthermore, with respect to the DSC calculations given earlier, MADS occurs in 2015 at about \$209 million, dropping immediately in the following year to less than \$100 million and remaining steady at about \$110 million thereafter; this drop is due to 2015 being the final payment for 1998TA GANs, and we reiterate this will be prefunded by June 2014.

In our view, potential delays in authorizations, changes in law, declining highway trust fund balances, or Congressional or administrative modifications to grant programs will not end the longstanding practice of federal aid for transportation on which we base our grant anticipation ratings. However, program rule changes, constrained funding sources, and federal budget pressures could lead to lower authorization and appropriation levels and diminish coverage, which we currently view as very strong for most transportation grant-backed bonds we rate. Weaker or varying levels of appropriations could reduce the overall level of support and predictability associated with the grant programs, which, in turn, could affect our ratings. We do not expect rating changes to grant-anticipation programs

such as Massachusetts' that benefit from a security pledge of funds in addition to the federal aid revenues (enhanced or double-barreled GANs). As with other transportation grant-backed bonds, we consider Congress' passage of a new reauthorization program (MAP-21) to be a favorable development for the overall sector. While we note that the bill ensures funding only to Sept. 30, 2014, we expect that Congress will continue to provide extensions as needed to allow uninterrupted construction programs and debt service payments. Furthermore, the federal government shutdown did not affect U.S. Department of Transportation employees charged with administering payment under the highway program, and Massachusetts officials report that the commonwealth continued to receive about \$10 million a week during the period.

Finally, although we believe that federal sequestration may affect transfers from the federal general fund to the highway trust fund (the latter having relied on such transfers in recent years to remain solvent), we believe that any potential reductions will not affect overall credit quality given strong DSC and, in the case of Massachusetts, the added support of net CTF revenues.

Outlook

The stable outlook reflects our expectation that the long-standing federal aid highway program will continue to receive significant funding during the next two years and thereafter, and that Massachusetts will continue to receive its historical share of annual Title 23 distributions. Should there be a significant decline in DSC or should the state fail to prudently manage the reimbursement process, we could lower the rating. Our stable outlook is further predicated on net CTF funds continuing to provide sharply higher DSC when coupled with federal highway funds.

Related Criteria And Research

USPF Criteria: Methodology And Assumptions: Rating U.S. Federal Transportation Grant-Secured Obligations, May 29, 2009

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