S&P Global Ratings

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Massachusetts Bay Transportation Authority; Sales Tax

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Credit Profile		
US$95.0 mil subord sales tax bnds variable rate dem oblig (Massachusetts) ser 2022A due 07/01/2052		
Long Term Rating	AA/A-1+/Stable	New

Credit Highlights

- S&P Global Ratings assigned its 'AA/A-1+' dual rating to the Massachusetts Bay Transportation Authority's (MBTA) $95 million subordinated sales tax bonds, variable-rate demand obligations (VRDOs), 2022 series A.
- The long-term component of the rating reflects credit characteristics of MBTA's pledged revenue.
- The 'A-1+' short-term component of the rating on the bonds reflects our assessment of the liquidity enhancement in the form of a standby bond purchase agreement (SBPA) from TD Bank N.A., the SBPA provider.
- The outlook on the rating is stable.

Security

The series 2022A sales tax bonds and parity debt, subordinate to the senior sales tax bonds, are secured by a gross pledge of the greater amount of either a statewide sales tax defined as a 1% statewide sales tax, which excludes sales tax on meals, plus $160 million of additional state sales tax per year that MBTA receives for operational funding; or an inflation-adjusted sales tax revenue base amount distributed by the Commonwealth of Massachusetts. The senior sales tax pledge is subordinate to the prior closed-lien general transportation bond obligations outstanding issued before July 2000, to the extent that MBTA does not certify that its general revenues can cover these prior-lien obligations in its annual budget from general revenues. In addition, pledged to the senior sales tax bonds are surplus assessments on 176 cities and towns, after payment of debt service on separate MBTA assessment bonds that have a first lien on those revenues. We understand that both the pledged dedicated sales tax amount and the base amount do not need a legislative appropriation to be used to pay debt service.

The 2022 series A VRDOs are being issued to fund a portion of the authority's capital improvement program (CIP).

The bonds are being issued as VRDOs and will receive liquidity support in the form of standby bond purchase agreements (SBPAs) from TD Bank effective Sept. 28, 2022. The SBPA will cover principal and 187 days' interests at a maximum 10% annual rate for the purchase price of bonds that are not successfully remarketed. The SBPA is due to expire on Sept. 27, 2027, unless extended or terminated beforehand.

Credit overview

The long term component of the MBTA sales tax bond ratings are based on what we perceive to be the stronger pledge of either the state-guaranteed base revenue amount or pledged MBTA sales tax revenue. Currently, we view the pledge of state-guaranteed base revenue amount as having a stronger credit quality as it is backed by the commonwealth's guarantee of all sales tax Massachusetts collects. The subordinate sales tax bonds outstanding will continue to have an open lien permitting additional debt issuance using the same additional bonds test (ABT) coverage multiple; as a consequence, we expect debt service coverage (DSC) based on pledged revenue to remain strong and of similar magnitude in the near term for all liens. We believe the lack of a debt service reserve (DSR) on the subordinate bonds is mitigated by strong DSC levels.

The short-term component of the rating reflects the liquidity facility in the form of an SBPA provided by TD Bank effective on Sept. 28, 2022. It is our understanding that the bonds will initially be issued in the weekly rate mode. They are subject to mandatory tender before conversion to any other mode. The SBPA covers the bonds in the weekly and daily rate modes.

The SBPA provider's obligation to purchase unremarketed tendered bonds while the bonds bear interest in the weekly or daily rate mode (the covered modes) will terminate without notice to bondholders should various events, as outlined in the SBPA, occur. These events, which we consider consistent with our published criteria, include, but are not limited to, lowering of the long-term component of the rating on the bonds below 'BBB-'.

Massachusetts' 'AA' general obligation (GO) rating reflects a strong economy, with the second-highest per capita income level in the nation, partly due to an above-average presence of high-technology companies in the Boston metropolitan statistical area (MSA). The rating further reflects some historical cyclicality in financial results, although recent strong growth in tax collections and federal aid have led to large operating surpluses and reserves, as well as high debt, pension, and other postemployment benefit (OPEB) liabilities, with a history in recent years of funding less than full annual actuarial recommendations to its pension and OPEB funds.

So far in fiscal 2023, Massachusetts's revenues have continued to come in much better than the budgetary forecast. Through August 2022, fiscal 2023 tax collections for the year to date were up 5.2% over the same period the prior year. Strong recent tax growth has swelled the commonwealth's budget stabilization fund (BSF) balance, which receives both excess general fund revenue, as well as capital gains tax above an annual benchmark, and certain other lesser revenue sources. The commonwealth's BSF is estimated at $6.9 billion, or a very strong 10.0% of expenditures and other uses at the end of fiscal 2022. Its enacted fiscal 2023 budget projects that the BSF will increase to $8.4 billion at the end of fiscal 2023.

Factors supporting the 'AA' GO rating include what we view as Massachusetts':

- Deep and diverse economy;
- High income levels, with per capita income at 132% of the nation in 2021, the second-highest among the states;
- History of timely monitoring of revenues and expenditures and swift action when needed to make adjustments;
- Strong financial, debt, and budget management policies, including annualized formal debt affordability statements and multiyear capital investment planning; and
- Strong BSF balance, equal to about 10% of expenditures and other uses on a budgetary basis at fiscal year-end 2022, in part due to currently strong capital gains tax.

Offsetting factors include high debt, pension, and OPEB liabilities.

For more information on the commonwealth, please refer to our most recent summary analysis on Massachusetts, published Jan. 20, 2022, on RatingsDirect.

Environmental, social, and governance

In our view, environmental, social, and governance (ESG) risks reflect those of the Commonwealth of Massachusetts as it pertains to sales tax collection. We consider Massachusetts' environmental risks moderately negative to our credit analysis because of its coastal exposure, with about two-thirds of its population in the Boston MSA and substantial property value in the combined Boston and Cape Cod area. We view social and governance as neutral to the credit analysis.

For more information about the Massachusetts' ESG risks, please refer to our "ESG Credit Indicator Report Card: U.S. States And Territories," published March 31, 2022, on RatingsDirect.

Outlook

The stable outlook reflects our stable outlook on the commonwealth's GO rating and our view of MBTA's ability to issue future additional parity bonds under its senior- and subordinate-lien ABTs based on the size of base revenue amount. Our outlook also assumes consistently strong DSC over our two-year outlook horizon despite capital pressures.

Downside scenario

Should we lower our GO rating or revise our outlook on the commonwealth, we could potentially lower our ratings on the MBTA sales tax bonds and the TIFIA/RRIF loans. Significant additional debt leverage that lowered DSC closer to the 1.5x sales tax coverage test portion of the ABT, or a debt structure that included a significant amount of variable-rate or short-term debt in a rising interest rate environment, could also result in our lowering the rating or revising the outlook to negative.

Upside scenario

The rating is limited by our view of Massachusetts' creditworthiness and is constrained at the current level unless the commonwealth GO rating is raised, despite strong DSC. However, if we believe the creditworthiness of MBTA's direct sales tax pledge strengthens enough so that it is stronger than the pledge of the base revenue amount and the ABT provisions are strengthened and we view DSC will likely be sustained at very strong levels on outstanding and future debt, we could raise our ratings above the state's GO.

Credit Opinion

Subordinate bonds sales tax pledge

Parity sales tax bonds issued since July 1, 2000, have been backed by a lien on the 1% statewide sales tax (which excludes sales tax on meals) plus $160 million per year of commonwealth's sales tax, subordinate to the prior-lien bonds issued before 2000, with excess sales tax revenues funding subordinate debt service and MBTA general operations.

The 1% pledged sales tax, plus $160 million per year, are part of the commonwealth's overall 6.25% sales tax rate. Sales tax revenue declined in the Great Recession, with a cumulative decline of 7.9% in fiscal years 2008-2010. However, as Massachusetts' economy recovered, sales tax has since risen, increasing 0.3% most recently in fiscal 2022.

Although current DSC is strong, we believe coverage could potentially drift downward again closer to the ABT, as occurred before the 2015 addition of the extra $160 million pledge to the bonds of state sales tax on a gross basis that is used for MBTA operations, in light of the large CIP, and the potential for cost overruns or expanded borrowing. The subordinate bonds will not have a DSR. MBTA is in process of gathering bondholder consent to convert the senior bond debt service requirement into an aggregate amount, instead of a per series requirement, by voting new bond issues in favor of the amendment.

Combined MADS coverage from all liens on general transportation revenue bonds, senior and subordinate sales tax bonds is very strong, in our opinion, at what we calculate as 2.7x by historical fiscal 2022 pledged actual sales tax revenues, and 2.6x by the 2022 certified state-guaranteed base revenue amount. MBTA anticipates about $4.4 billion in additional debt in its current CIP through 2027.

The ABT requires all bonds to meet the subordinate ABT. The ABT requires either 1.0x coverage of combined prior general transportation bonds and combined senior and subordinate sales tax bond MADS by the base revenue amount, or 2.0x coverage by historical sales tax revenues, net of prior general transportation bond debt service; and 1.5x coverage of sales tax revenue bond debt service and all prior general transportation debt obligations on a combined basis by historical sales tax revenue.

Base reserve amount

The commonwealth created a formula for a guaranteed base amount of pledged sales tax revenue should pledged sales tax revenue decline, or not increase as fast as inflation. This base amount was raised by an extra $160.0 million in fiscal 2015, and subsequently increases annually by the rate of the Boston CPI up to 3% per year, or lower to the extent that the rate the CPI increases is less than 3% but more than the sales tax rate increase (in which case the base amount increase is the rate of increase in sales tax). If neither the CPI nor the sales tax increase in a given year, the base amount is held flat for that year. The base amount has increased to $1.128 billion, due in fiscal 2023, compared with $787 million in 2013. MBTA also receives other commonwealth money and federal revenues that are not pledged to the sales tax bonds.

Variable-rate debt and swaps

The authority expects to have $125.6 million of unhedged sales tax VRDOs and authorization for up to $400 million of CP bond anticipation notes, all secured by sales tax revenue, which will make up about 11.8% of total sales tax-secured debt.

MBTA has an interest rate swap agreements associated with about $79.7 million of variable-rate sales tax-secured bonds. The authority is not required to begin posting collateral for any of its swap agreements in the event of negative swap valuations until the sales tax rating on MBTA falls below 'A'. Immediate swap termination events with notice do not go into effect unless the rating on MBTA or Massachusetts falls below 'BBB-', although certain swap termination events with notice can occur if the sales tax rating falls below 'A-'. Any swap termination payments would be subordinate to payment of sales tax bond debt service. We believe that termination events are unlikely at current rating levels.

MBTA Operations

MBTA runs the oldest and fifth-largest transit system in the country, operating subway, bus, and commuter rail service throughout eastern Massachusetts. Prior to the COVID-19 pandemic, it was responsible for an estimated 1.3 million passenger trips each business day and operates more than 38 miles of rapid-transit rail routes, and 26 miles of additional light rail. In addition, MBTA provides a broad range of other passenger services, including commuter boats. Its territorial area has increased to 175 cities primarily in the greater Boston MSA, extending north to the New Hampshire border, west to the city of Worcester, and south into Providence, R.I., with a total service area population of about 4.8 million.

The COVID-19 pandemic severely affected MBTA's operations, with an almost 80% reduction in fares. As a result, the authority had a budget deficit in fiscal 2021 which exceeded $600 million before emergency federal assistance. The authority has received substantial federal stimulus funding related to the pandemic, including approximately $827 million from the 2020 Coronavirus Aid, Relief, and Economic Security (CARES) Act, approximately $301 million from the Coronavirus Response and Relief Supplemental Appropriations Act of 2021, and approximately $860 million from the American Rescue Plan Act of 2021. The federal aid is expected to be used through fiscal 2024 to pay operating costs to maintain service and to make up for lost revenue due to the COVID-19.

In fiscal 2021, the last audited year, MBTA operating expenses less depreciation were $1.7 billion; this does not include debt service, which is deducted from sales tax before being credited to operating funds. Its unrestricted cash and temporary cash investment position was $647.9 million at fiscal year-end June 30, 2021. Like most transit systems, MBTA relies heavily on intergovernmental operating subsidies to pay for operations. The 2021 Transportation Bond bill was enacted by the legislature to provide nearly $5.1 billion in capital support for the authority. The 2021 Transportation Bond bill was enacted by the legislature to provide nearly $5.1 billion in capital support for the authority.

MBTA was created in 1964, and was put under the control of a state oversight board following various operational issues in the winter of 2015. The oversight board expired June 30, 2021. Following dissolution of the control board, MBTA governance devolved onto the Massachusetts Department of Transportation (MassDOT), although MBTA exists as a separate legal entity within the department. However, subject to the enabling act amendment in 2021, MBTA has a separate seven-member governing board, five of whom are appointed by the governor. The enabling act does not provide for MBTA to be a debtor under the federal bankruptcy code.

It estimates a five-year 2023-2027 MBTA CIP of $9.4 billion. The CIP includes a portion of the funding of the authority's $2.6 billion Green Line rail extension, which will also receive funding from federal and local sources. MBTA expects approximately $4.3 billion of its current five-year CIP will be funded with its own sources, $1.2 billion from state rail enhancement bonds, and $3.7 billion from federal assistance.

Massachusetts Bay Transportation Authority Pledged Revenues

Fiscal year	Total statewide sales tax receipts ($000s)*	MBTA carve-out of total sales tax receipts ($000s)§	% increase (decrease)§	Base revenue amount (BRA) (floor) ($000s)§	Difference in BRA versus dedicated 1%
1996	2,252,083	450,417	5.4	N/A	N/A
1997	2,494,702	498,940	10.8	N/A	N/A
1998	2,572,560	514,512	3.1	N/A	N/A
1999	2,833,644	566,603	10.1	N/A	N/A
2000	3,108,430	621,433	9.7	N/A	N/A
2001	3,273,817	654,591	5.3	645,000	9,591
2002	3,193,947	638,789	-2.4	664,350	(25,561)
2003	3,196,009	639,202	0.1	684,281	(45,079)
2004	3,211,141	642,228	0.5	684,281	(42,053)
2005	3,330,838	666,167	3.7	704,809	(38,642)
2006	3,420,209	684,042	2.7	712,586	(28,544)
2007	3,458,885	691,777	1.1	733,963	(42,186)
2008	3,453,776	690,755	-0.1	755,982	(65,227)
2009	3,239,083	647,817	-6.2	767,057	(119,240)
2010	3,852,057	637,084	-1.7	767,057	(129,973)
2011	4,091,485	654,643	2.8	767,057	(112,414)
2012	4,190,558	670,494	2.4	779,092	(108,598)
2013	4,262,750	682,046	1.7	786,867	(104,821)
2014	4,546,992	727,519	6.7	799,295	(71,776)
2015	4,775,641	924,103	27.0§	970,637§	(54,942)
2016	4,990,760	958,522	3.7	986,274	(27,752)
2017	5,104,756	976,761	1.9	992,192	(15,431)
2018	5,299,437	1,007,910	3.2	1,006,807	1,103
2019	5,582,310	1,053,170	4.5	1,032,068	21,102
2020	5,733,174	1,077,308	2.3	1,063,030	14,278
2021	6,883,820	1,261,411	17.1	1,083,333	178,078
2022		1,265,728	0.3	1,095,608	170,120

*Total state sales tax rate was 5.00% until 2009, when it increased to 6.25%. §Pledged sales tax was equal to a 1% rate until 2015, when it was increased to 1% plus $160 million per year; 2015 increase without extra $160 million would have been 5.0%. The BRA floor amount is established by the state comptroller each year using a formula including CPI index. By law, the BRA formula cannot increase more than 3% annually, except it was also increased $160 million in 2015. N/A--Not applicable. Source: Massachusetts Department of Revenue.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022
- ESG Credit Indicator Report Card: U.S. States And Territories, March 31, 2022