S&P Global
Ratings

RatingsDirect®

Connecticut; Gas Tax

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Credit Profile		
US$800.0 mil spl tax oblig bnds ser 2016A due 09/01/2036		
Long Term Rating	AA/Stable	New
US$200.0 mil spl tax oblig rfdg bnds ser 2016B due 09/01/2028		
Long Term Rating	AA/Stable	New
Connecticut sr lien gas		
Long Term Rating	AA/Stable	Affirmed

Rationale

S&P Global Ratings has assigned its 'AA' long-term rating, and stable outlook, to the State of Connecticut's $800 million series 2016A special tax obligation (STO) bonds for transportation infrastructure purposes, and $200 million series 2016B STO refunding bonds for transportation infrastructure purposes. At the same time, S&P Global Ratings has affirmed its 'AA' rating on the state's STO senior parity bonds ($4.2 billion) and second-lien bonds ($257.4 million). The outlook is stable.

The STO bonds are secured by a first-lien pledge of revenues to the Special Transportation Fund (STF), paid before transportation operations. According to bond counsel, the funds are deemed to be appropriated each year and no further legislative approval is required.

We base our ratings on our assessment of the following factors:

- A diverse mix of pledged revenues, in our view, that are levied on a large statewide economic base (population: 3.6 million);
- Connecticut's history of adding to pledged revenues when it has increased the size of its transportation capital program, as evidenced by increased allocation of state sales tax beginning in fiscal 2016;
- Strong 2.45x coverage of future maximum annual debt service (MADS) after this issuance by state-estimated fiscal 2016 pledged revenues on combined senior- and second-lien bonds, excluding Build America bonds (BABs) interest subsidy and fund interest earnings, and 2.82x coverage on senior-lien MADS alone;
- State projections for annual debt service coverage (DSC) of more than 2.5x for senior-lien bonds, and more than 2.3x annual DSC on combined senior- and second-lien bonds after expected future debt issuances, through at least fiscal 2020, including BAB subsidies and interest earnings; and
- Strong bond provisions, including a 2.0x additional bonds test (ABT) for both first- and second-lien bonds, coupled with a fully funded debt service reserve account, and a 2.0x rate covenant.

Credit risks include what we consider:

- A sizable, but well-defined, capital improvement program that includes $2.7 billion of planned additional new money bonds through fiscal 2020, and the potential for substantially more bonding after 2020 to the extent pledged revenue is increased in future years; and
- A pledged revenue stream that is somewhat susceptible to economic conditions related to changes in the price and availability of motor vehicle fuel and motor vehicle sales, or potential changes in statutory funding formula. In fiscal

2016, the state delayed the deposit of pledged sales tax to the STF for two months ($35.2 million) to help balance state general fund operations, and reduced the sales tax deposit by $50 million in fiscal 2017, equal to about 3% of total pledged STO revenue.

We understand that proceeds from this bond issue will be used to fund various projects included in the transportation infrastructure program, and refund certain outstanding senior-lien bonds.

The senior-lien bonds are secured by a first-lien pledge on funds deposited in the STF and paid before operating expenditures. The second-lien bonds are payable after required payments on the senior-lien bonds, in advance of funding operations. The indenture also requires that as long as the second-lien bonds are outstanding, after deducting for required reserves, pledged revenues for both liens must equal at least 2x annual debt service requirements. Because the structure of the second-lien bonds is the same as the senior-lien bonds, except for the flow of funds, and debt service coverage (DSC) is strong, in our view, we do not make a rating distinction between senior- and second-lien bonds outstanding. All STO bonds are fixed rate.

The state has made changes in its allocation of pledged revenue to the STF in recent years that in general has increased the overall amount of STO pledged revenue, which has supported an expansion of its transportation capital plan.

Beginning in fiscal 2016, Connecticut made a statutory dedication of a certain portion of its statewide general sales tax to the STF. The dedicated allocation grows over time, with a full 0.5% statewide dedicated sales tax to be fully phased in by fiscal 2018. However, we believe pledged revenues will remain diverse. Sales tax is projected to be about 21% of pledged revenues in 2018, not including another 6% of pledged revenue attributable to a previous dedication of sales tax from casual car sales between individuals. In our view, sales taxes have the potential to show more variation over the economic cycle than per gallon fuel taxes or motor vehicle license fees, but they are also likely to grow faster over time.

Estimated actual fiscal 2016 STF revenue currently comprises what we view as a diverse mix of motor fuels taxes (38% of estimated fiscal 2016 pledged revenues and 30% of 2018 revenue based on state projections); oil companies' tax payments (18% in 2016 compared with 21% in 2018); motor vehicle receipts (18% in 2016 compared with 16% in 2018); and licenses, permits, and fees (11% in 2016 compared with 9% in 2018), not including the effects of legislative net fund transfers and refunds. Pledged revenues also include BAB federal interest subsidy payments and fund interest income.

While we expect revenues overall to increase with the additional sales tax, the STF experienced a small 1.5% dip in total pledged revenue in fiscal 2016 due to lower oil company tax revenues, and a two-month $35.2 million delay in the allocation of sales tax to the STF in order to provide general fund budget relief. There was a further $50 million budgeted reduction in sales tax allocated to the STF in fiscal 2017, also for budget relief. We believe that the state could make additional STF allocation reductions in future years as the result of state budget stress (Connecticut GO rating: AA-/Stable), but expect these transfers to remain relatively minor due to the need to fund ongoing transportation operations. The $50 million reduction in allocated sales tax in fiscal 2017 represents only about 3% of total projected STF revenue. In previous years, the state has made other transfers and allocations to and from the STF of a one-time nature, but overall we believe pledged revenue has remained relatively stable and annual DSC strong.

Legal covenants include a 2.0x annual DSC rate covenant.

We calculate estimated pledged revenues collected by the state comptroller for the fiscal year ended June 30, 2016, not including pledged BAB interest subsidy or interest earnings, covered proposed future senior-lien MADS of $473.1 million occurring in fiscal 2018 after this sale by 2.82x, and combined senior- and second-lien MADS by 2.45x also in 2018.

The state projects annual DSC will remain above 2.5x through 2020, despite plans to issue $2.7 billion of new money STO through fiscal 2020, in part due to the phase in of the additional sales tax as pledged revenue, and due to a currently declining debt service schedule after fiscal 2018. The additional sales tax revenue added in 2016 is part of the state's new 30-year Let's GO CT! infrastructure plan that could eventually involve as much as $100 billion of debt. However, the state expects that substantial bonding beyond 2020 would be met with additional pledged revenue not currently in statute, which could also potentially replace a portion of existing revenues. The increased allocation of sales tax to the STF represents the first five years of this long-term goal. Connecticut has historically maintained annual DSC above the 2.0x ABT requirement, ranging from 2.9x-3.7x for senior-lien bonds and 2.5x-3.0x for combined senior- and second-lien bonds since fiscal 2009. After issuance of the series 2016 bonds, the state will have $4.0 billion of authorized but unissued STO bonds.

(For more information on the state and its economy, please refer to the most recent state GO summary analysis published May 19, 2016, on RatingsDirect).

Outlook

The stable outlook reflects S&P Global Ratings' view that the financial integrity of the fund and strong DSC levels will continue over the two-year outlook horizon. Economic trends are stable and increased sales tax revenue is currently being phased into the pledged STF to offset expansion of the transportation capital program. We believe planned additional bonding will eventually lead to somewhat lower annual DSC levels beyond our two-year outlook horizon, while remaining above levels that we would consider strong. If DSC weakens significantly, or the historical state focus on the integrity and support for the STF weakened so as to deplete STF resources in a significant manner, we could potentially lower the rating or revise the outlook on the bonds. We do not see the potential for a higher rating in the next two years given the sizable projected debt issuance and the legal ability of the state to reduce future allocations of pledged revenue up to its 2x rate covenant.

Bond Structure

Bond provisions are strong in our view. The senior-lien bonds are secured by a first-lien pledge on funds deposited in the STF and are paid before operating expenditures. The ABT requires 2x coverage (based on an historical earnings test adjusted for approved tax rate increases or decreases) of all senior- and second-lien debt. The second-lien indenture also requires that as long as second-lien debt remains outstanding, DSC for both liens must at least be equal to 2x annual debt. In addition, the debt service reserve fund must be funded at an amount equal to the MADS on the bonds outstanding. The debt service reserve fund is held with a trustee and is a combined debt service reserve available for both the first- and second-lien bonds.

The state has also covenanted in both the senior- and junior-lien indentures to levy sufficient taxes and fees to provide DSC, and to provide sufficient pledged revenue so as to provide 2.0x annual DSC at the end of each fiscal year. Failure to provide such coverage, however, is not an event of default unless the state shall not enact legislation that would satisfy indenture covenants if additional debt were then to be issued.

Connecticut -- Special Tax Obligation Bond Debt Service Coverage

	--Actual--					
(Mil. $)	**2013**	**2014**	**2015**	**2016e**	**2017p**	**2018p**
Motor fuels tax	501.3	508	516.6	518.2	503.7	506.8
Oil companies tax	199.4	380.7	337.9	250	268.4	298.8
State sales tax	0	0	0	109	202.9	348
Motor vehicle receipts	234.5	236.1	249.5	251.5	261.8	263.5
License, permits, fees	137.3	138.4	145.4	145.3	141.5	142.0
Sales tax - DMV	79	82.2	83.9	87.2	90.3	90.9
Federal grants (BAB subsidy)	12.4	12.1	12.1	12.2	12.1	12.1
Interest income	4.1	6.8	6.9	7.8	8.5	9.5
Transfers from/(to) other funds	88.7	(83)	34.7	(6.5)	(6.5)	(6.5)
Transfers to Transportation Strategy Board (TSB) (eliminated in 2016)	(15)	(15)	(15)	0.0	0.0	0.0
Total revenues	1,241.7	1,266.3	1,372.0	1,374.7	1,482.7	1,665.1
Refunds	(9.2)	(10.6)	(11.1)	(20.8)	(18.3)	(16.5)
TSB projects account transfers added back in	15.0	15.0	15.0	0.0	0.0	0.0
Total pledged revenues	1,247.5	1,270.7	1,375.9	1,353.9	1,464.4	1,648.6
Pledged revenue without BAB subsidy or interest income	1,231.0	1,251.8	1,356.9	1,333.9	1,443.8	1,627.0
Senior-lien MADS in 2018 after this sale	473.1	473.1	473.1	473.1	473.1	473.1
Combined senior- and second-lien MADS in 2018 after this sale	544.1	544.1	544.1	544.1	544.1	544.1
Coverage of senior-lien MADS alone ($473.1 million in fiscal 2018) without BABs (x)	2.60	2.65	2.87	2.82	3.05	3.44
Coverage of combined senior- and second-lien MADS ($544.1 million in fiscal 2018) (x)	2.26	2.30	2.49	2.45	2.65	2.99

DMV--Department of Motor Vehicles. BAB--Build America bonds. MADS--Maximum annual debt service. e--Estimated. P--Projected.

Transportation Overview

The Department of Transportation (DOT) was established in 1969, and replaced the Connecticut Highway Department. The DOT is headed by a commissioner appointed by, and reporting to, the governor. Total employment as of July 22, 2016, was 3,060 employees, up from 2,789 in 2011, but similar to 2,964 in 2010. The state's transportation system includes roads (21,508 miles, of which approximately 4,143 are maintained by the DOT), state and local bridges (5,296), commuter rail, a bus system, and Bradley International Airport. The transportation infrastructure program was established in 1984 and has financed a broad range of projects across Connecticut. Total funding from 1985-2020 is estimated at $37.8 billion and includes federal state and local funds, with the state's share estimated at $18.6 billion, of which $17.8 billion is to be financed by bonds. Connecticut expects to issue about $900 million annually of additional new money STO bonds from fiscal 2018 through fiscal 2020.

Financial Update

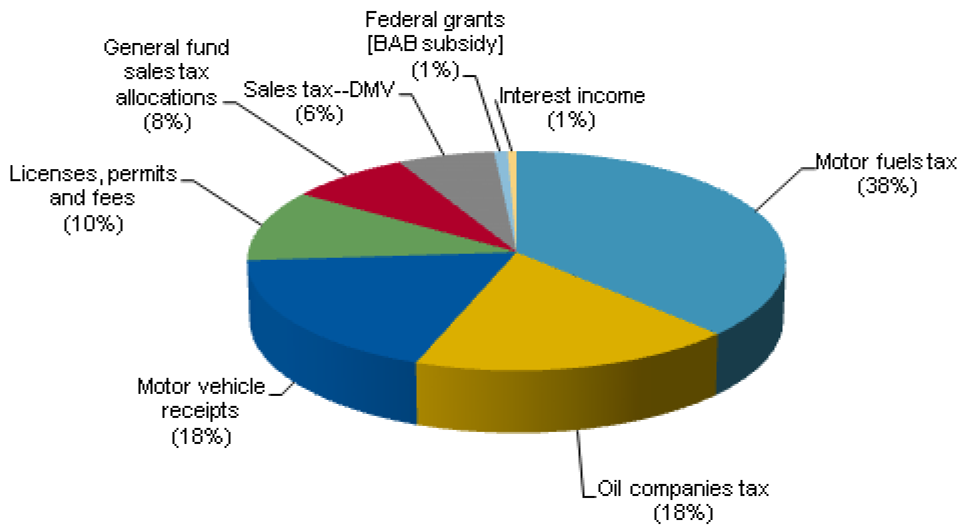
The state estimates that the STF recorded a $29.6 million operating deficit in fiscal 2016, the first operating deficit since 2009, and following an operating surplus of $11.0 million in fiscal 2015 and $4.4 million in 2014. Connecticut projects operating surpluses in fiscal years 2017-2019, before another $56.2 million deficit in fiscal 2020. However, the state throughout this period projects that its STF cumulative fund balance will remain above at least $150 million. At fiscal year-end 2016 it was just at this level--$150.4 million, or 10.9% of STF expenditures. As the size of the capital plan has increased, various legislative changes have been made over time to address projected shortfalls and support increased debt authorization including changes in fiscal years 2009 and 2016 to enhance the fund with additional transfers from the general fund. Ongoing budget pressure in the general fund subsequently reduced the amount of these transfers. In fiscal 2014, a one-time $76.5 million transfer was made from the STF to the general fund, offset by oil company taxes transferred to the STF, which are now deposited directly to the STF. In fiscal 2016, Connecticut delayed deposit of sales taxes by two months into the STF to provide $35.2 million of state budget relief, and another $50 million transfer to the state general fund in fiscal 2017. However, overall Connecticut projects that $348 million of new state sales tax will be directed into the STF in fiscal 2018, when the full 0.5% statewide sales tax allocation will be phased into the STF per statutory law.

Major revenue enhancements to the fund over the years have included:

- The allocation of a portion of Connecticut sales tax, which is expected to phase in over time until 0.5% sales tax is dedicated to the STF in 2018;
- The oil companies tax (of which all is now transferred directly to the STF as a statutory allocation, instead of being transferred from the general fund);
- Motor vehicle fee increases in previous years; and
- A motor fuels tax increases in previous years.

The transfers and revenue enhancements that Connecticut has planned are projected to contribute to surplus operations after payment of DOT expenses through 2019.

Connecticut
Fiscal 2016 estimated pledged revenues before transfers and refunds



DMV--Department of Motor Vehicls. BAB--Build America bonds.

Ratings Detail (As Of September 2, 2016)

Connecticut gas (AMBAC) (MBIA)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut spl tax oblig bnds		
Long Term Rating	AA/Stable	Affirmed
Connecticut spl tax oblig bnds transp infrastructure purp		
Long Term Rating	AA/Stable	Affirmed
Connecticut 2nd lien		
Long Term Rating	AA/Stable	Affirmed
Connecticut special Tax Gas		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut Special Tax Gas		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.