S&P Global
Ratings

RatingsDirect®

Summary:
Vermont; Gas Tax

Primary Credit Analyst:
Jillian Legnos, Boston (1) 617-530-8243; jillian.legnos@spglobal.com

Secondary Contact:
Sussan S Corson, New York (1) 212-438-2014; sussan.corson@spglobal.com

Table Of Contents

Summary:

Vermont; Gas Tax

Credit Profile		
Vermont Gas Tax		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'AA+' rating on the State of Vermont's special infrastructure bonds outstanding. The outlook is stable.

The bonds are secured under a trust indenture by pledged revenues primarily consisting of a 2% assessment of the retail price per gallon of regular gasoline, excluding state and federal taxes, and a three-cent-per-gallon assessment on diesel fuel. State statutes prevent the pledged assessment rates from being reduced while the bonds are outstanding.

In the 2015 legislative session, state lawmakers amended the prevailing statute to establish a floor to collect at least 3.96 cents per gallon from the 2% retail price per gallon gasoline assessment. Officials estimate that the floor, which was established following a decline in gas prices, would take effect when the retail price drops below approximately $2.50 per gallon.

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

- The broad-based, statewide nature of motor fuel tax revenues;
- Revenue collections that benefit during periods of rising gasoline prices and that are exposed to limited risk from falling gasoline prices,
- Strong 6.0x coverage of maximum annual debt service (MADS) in fiscal 2016;
- A good senior-lien additional bonds test (ABT) requiring at least 2.0x debt service coverage to issue additional parity debt; and
- Approximately level debt service schedule, with all principal to be retired by 2033.

The assessment on gasoline sales, which have historically represented about 90% of total pledged revenues, is dependent both on consumption trends and retail prices. Consequently, total pledged revenues supporting the bonds have reported volatility that we believe is characteristic of the revenue pledge. In the six years that pledged revenues have been authorized and collected, revenues have generally mirrored trends in retail gasoline prices, in our opinion. Total pledged revenues rose 37% from $14.7 million in fiscal 2010 to a peak of $23.0 million in fiscal 2013. Three years later, revenues sit 35% lower than the fiscal 2013 peak at $14.9 million in fiscal 2016. The state reported this significant decline in revenues while the consumption in the same time period fell only 1.7%, according to data from the Vermont Legislative Joint Fiscal Office.

Coverage trends have reflected revenue collections with MADS coverage rising from 5.9x in fiscal 2010 to a peak of 9.2x in fiscal 2013, and declining to 6.0x in fiscal 2016. However, we consider this level of coverage to be very strong and expect it to remain so in the future. According to our calculations based on fiscal 2016 consumption data, coverage based on revenues hitting the collection floor would provide 5.7x MADS coverage for combined gasoline and diesel fuel collections and 4.9x MADS coverage for gasoline collections alone. We consider this level of coverage to be very strong. In our opinion, the juxtaposition of consumption and collection trends demonstrates the inherent volatility of the revenue pledge. However, we believe the downside risk from such volatility is mitigated given the establishment of the gasoline assessment collection floor. We view this amendment as important to the rating given that a major component of the pledged revenue base exhibits a propensity for volatility. In addition, we note that collections should increase during periods of rising gasoline prices, which we consider a credit strength.

We expect gasoline prices to stabilize or rise in the next several years given our assumptions regarding crude oil prices. S&P Global Ratings recently raised its assumption for Brent and West Texas Intermediate crude oil for 2017 to $50 a barrel from $45 a barrel. We expect crude oil prices will stabilize in 2018 and rise to $55 in 2019 and beyond. (For more information, please see the most recent oil and natural gas commentary "S&P Global Ratings Raises Its Oil And Natural Gas Prices Assumptions For 2017," published Dec. 14, 2016, on Ratings Direct.)

The debt service reserve is required to be equal to the standard three-part test of 100% of MADS, 125% of average annual debt service, or 10% of par. According to our calculations, the reserve will be maintained at level at least equal to MADS. Under the trust agreement, the collections are deposited in the revenue account, transferred to the debt service fund, then transferred to the paying agent for payment of debt service. There is no annual appropriation risk.

The ABT requires 2x MADS coverage by historical revenues in 12 consecutive months out of the previous 18. The test allows for the projection of an increase in revenues from any subsequent additions to the revenues pledged to the parity debt

Officials do not expect to issue additional parity debt at this time. However, the program is regularly evaluated. The new administration under Governor-Elect Phil Scott is currently working on a capital plan but the timing of its release is unknown at this time.

The Vermont legislature authorized the fuel assessment in 2009 to address its construction needs for roads, bridges, and other transportation projects through pay-as-you-go capital expenditures or the issuance of motor fuel assessment bonds. The legislature has historically authorized three bond issues backed by these motor fuel assessments in fiscal years 2010, 2012, and 2013.

Outlook

The stable outlook reflects our expectation that MADS coverage will remain strong during our two-year outlook horizon as oil and gasoline prices stabilize or recover. The outlook also incorporates our expectation that the state will not bond down to the ABT based on current capital plans. Although not expected, significant declines in coverage could exert pressure on the rating. Should the gasoline assessment floor be appealed or amended in a manner we view as increasing Vermont's exposure to volatile gasoline prices, we could lower the rating. Barring structural changes that we believe would provide stability to volatile revenue collections, we do not expect to raise the rating during the two-year outlook horizon.