



**MASSACHUSETTS DEPARTMENT OF TRANSPORTATION**

**DEBT ISSUANCE AND MANAGEMENT POLICY**

**February 10, 2016**

## **1. Purpose**

The purpose of this policy is to establish a framework for the issuance and effective management of the debt of the Massachusetts Department of Transportation (“MassDOT”) consistent with Chapter 6C of the Massachusetts General Laws (the “Enabling Act”) and other applicable law and the terms of the relevant trust agreements. The policy is intended to serve as a source of information and guidance for the ongoing management of existing debt for the professional staff of MassDOT, its Board of Directors, and the bond rating agencies, as well as the general public and financial institutions doing business with MassDOT.

## **2. Scope**

The policy describes the circumstances and methods by which debt will be managed by MassDOT, including managing credit facilities, liquidity facilities, and interest rate modes supporting its variable rate debt. The policy also describes the internal management and external professional services necessary to support MassDOT’s debt portfolio and the process which will be followed to procure these services. Although MassDOT will not be issuing additional new money bonds, it monitors and proactively manages its existing debt portfolio and may explore refunding opportunities pursuant to the refunding guidelines outlined in section 14 below. This policy addresses the process and controls to be utilized in performance of the related tasks.

## **3. Authority**

MassDOT was created in 2009 by Chapter 25 of the Acts of 2009 (as amended, the “Transportation Reform Act”) and is a body politic and corporate and a public instrumentality of The Commonwealth of Massachusetts (the “Commonwealth”). MassDOT is governed by a eleven-member board (the “Board of Directors” or the “Board”) appointed by the Governor. The Governor appoints a Secretary of MassDOT, who serves as MassDOT’s chief executive officer and serves as a member of the Board.

The Transportation Reform Act provided for the dissolution of the Massachusetts Turnpike Authority (the “Authority”) and the transfer of its assets, liabilities, obligations and debt, including debt outstanding under its trust agreements, to MassDOT. MassDOT assumed the rights, powers and duties of the Authority effective November 1, 2009 in accordance with the Transportation Reform Act.

The Authority issued bonds under two separate trust agreements; the Metropolitan Highway System Trust Agreement (the “MHS Trust Agreement”) and the Western Turnpike Trust Agreement (the “WT Trust Agreement”). The Metropolitan Highway System (the “MHS”) and the Western Turnpike (the “WT”) are assets of MassDOT and are housed within its Highways Division. Bonds issued under the MHS Trust Agreement financed capital projects and refinanced outstanding bonds related to the MHS. Bonds issued under the WT Trust Agreement financed capital projects and refinanced outstanding bonds related to the WT. Only

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revenues from the Accepted Metropolitan Highway System (as defined in the MHS Trust Agreement) and the Western Turnpike are pledged under the MHS Trust Agreement and WT Trust Agreement, respectively, as security for the bonds issued thereunder.

Under the Enabling Act, MassDOT's authority to issue debt for purposes related to the MHS and the WT is limited to the issuance of refunding bonds. This Debt Policy provides guidelines for effective debt management within MassDOT's legal authority.

There are eleven members of the Board of Directors. Ten members of the board are appointed by the Governor and the Secretary serves ex officio as chair. Four members will serve terms conterminous with the Governor, while the remaining six members will be appointed to four year term and are eligible for reappointment. Three members of the Board serve on the Finance and Audit Committee. The Finance and Audit Committee reviews the issuance and management of MassDOT debt, including the procurement of credit and liquidity agreements or direct purchase agreements to support variable rate bonds, remarketing agents, financial advisors, legal counsel, and other services and agreements related to MassDOT's ongoing debt portfolio. The Board of Directors authorizes the issuance or reissuance of or amendments to outstanding bonds, and approves contracts as needed to manage MassDOT's debt and as required in compliance with the Enabling Act and Board regulations.

The Secretary and Chief Executive Officer of MassDOT has overall responsibility for the day-to-day operations and management of MassDOT. Management of MassDOT's finances is delegated to the Chief Financial Officer who is primarily responsible for debt management. The Chief Financial Officer is also supported by the Deputy Chief Financial Officer and the Director of Revenue and Debt Management. The Director of Revenue and Debt Management has a staff that oversees principal and interest payments on debt as well as the reconciliation of all swap settlements.

#### **4. Legal Authorization and Debt Limits**

Although there are no constitutional limits on the amount of MassDOT debt, the Enabling Act limits the issuance of bonds secured by MHS or WT revenues by MassDOT to refunding bonds. The public private partnership provisions contained in Section 67 of chapter 6C of the Enabling Act authorize the issuance of bonds, but these bonds would not be secured by MHS or WT revenues.

The MHS Trust Agreement and the WT Trust Agreement contain financial covenants, including debt service coverage ratios. MassDOT staff will carefully monitor compliance with such covenants.

#### **5. Procedure**

MassDOT continues to manage its ongoing debt obligations, including variable rate bonds and potential refunding opportunities. This management requires procurement of professional

services, including outside legal counsel, financial advisor, underwriters and swap advisor services. MassDOT executes periodic transactions in the financial markets such as replacement of credit or liquidity facilities pertaining to bonds, remarketing bonds, the issuance of refunding bonds and the amendment of variable rate bond modes as authorized in the MHS Trust Agreement.

MassDOT will engage the aforementioned external professional resources as needed to assist in the management of debt through competitive selection processes as described in Section 6. Any reissuance of MassDOT debt, such as changing of credit or liquidity providers or variable rate modes, will be done on a negotiated or competitive basis, depending on market conditions, debt structuring issues, and other factors deemed appropriate by the Secretary/Chief Executive Officer and Chief Financial Officer.

The Finance and Audit committee will review and the Board of Directors will authorize any reissuance or amendment of outstanding bonds. The Board of Directors may delegate to MassDOT officers the authority to execute and deliver documents as required for debt management.

## **6. Method of Procurement**

In accordance with its procurement procedures, MassDOT periodically issues competitive Requests for Qualification/Proposal or otherwise engages professional services including for bond counsel, rebate compliance, financial advisors, investment advisor, swap advisor and underwriters.

## **7. Debt Affordability**

In addition to complying with the requirements of the Enabling Act and the financial covenants under the MHS Trust Agreement and WT Trust Agreement, MassDOT staff, led by the Chief Financial Officer, will manage its debt to ensure sufficient revenues to meet its financial obligations and manage variable rate bond obligations and associated interest rate swap agreements. Managing interest rate swaps is governed by a separate Interest Rate Swap Management Policy, as described in Section 12 of this Debt Policy.

## **8. Risk Management**

MassDOT will monitor its outstanding debt with respect to risks, including without limitation, exposure to variable rates, liquidity and credit providers, remarketing agents, investments, and investment providers. MassDOT has structured the credit facilities, liquidity facilities, and interest rate modes supporting its variable rate debt to include Letters of Credit, Standby Bond Purchase Agreements and Direct Purchase Contracts with multiple counterparties and termination dates, to create greater diversification of credit, counterparty, and rollover risk. The risks evaluated by MassDOT prior to each transaction include:

- (i) *Counterparty (concentration and credit) risk.* MassDOT will seek to diversify its exposure, subject to the terms of the existing swaps, to counterparties across its financial portfolio, including swap counterparties, credit providers on variable rate debt, investment providers, and other exposures as may be incurred when managing the financial operations of MassDOT. For example, the credit rating and headline risk of the bank providing liquidity in the form of a Letter of Credit or Standby Bond Purchase Agreement may on occasion adversely impact the interest rate on MassDOT's variable rate bonds as they are remarketed. Alternatively, Direct Purchase transactions eliminate this risk. MassDOT therefore has diversified its variable rate structures accordingly.
- (ii) *Market Pricing Risk.* MassDOT employs a variety of variable rate structures and seeks to stagger termination and renewal dates to avoid coming to market at an inopportune time with its entire variable rate portfolio.
- (iii) *Ineffective Hedging risk-* MassDOT staff, its financial advisor, and bond counsel will evaluate each structure to assure any associated hedges are aligned properly.

MassDOT, its financial advisor, and bond counsel will continually evaluate MassDOT's liquidity position, termination events, interest rate modes, and other factors, for Letters of Credit, Standby Bond Purchase Agreements, Direct purchases, and any associated swaps and institute such controls as recommended by its independent advisors, legal counsel, auditors, or in accordance with best practices deemed appropriate by the Chief Financial Officer. In addition, MassDOT will abide by all applicable Federal and State laws and regulations including, but not limited to, those promulgated through the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. 111-203, H.R. 4173) ("Dodd-Frank") and the State Finance and Governance Board established pursuant to Section 97 of Chapter 6 of the Massachusetts General Laws.

## **9. Debt Structuring**

MassDOT debt is outstanding in the aggregate principal amount of approximately \$1.94 billion. Bonds issued under the MHS Trust Agreement amortize through January 1, 2039. Bonds issued under the WT Trust Agreement amortize through January 1, 2017.

Credit enhancement, insurance or liquidity will only be used when the present value or anticipated savings (i.e., reduced interest expense) exceeds the cost of the enhancement. Call features, when applicable, will be evaluated by considering the relative value of future financing flexibility and the market's perception of any premium associated with a call.

The relative amount of unhedged variable rate, hedged variable rate, and fixed rate debt will be monitored consistent with the risk control strategies described herein. Unhedged variable rate debt may be considered and limited to the extent of offsetting natural hedges in MassDOT's financial profile.

### **10. Credit Rating Agency Management**

MassDOT seeks to maintain the highest credit ratings reasonably possible within its resources. As part of each bond issuance (including variable rate bond credit support renewals and replacements) or at least annually, MassDOT will provide updated information to the rating agencies in excess of that required as part of the ratings surveillance and assignment process.

### **11. Investor Relations**

MassDOT's most recent Official Statements and audited financials will be posted on its website ([www.MassDOT.state.ma.us](http://www.MassDOT.state.ma.us)). MassDOT also will submit annual filings, significant event notices and any other voluntary or interim disclosure to the Electronic Municipal Market Access ("EMMA") system operated by the Municipal Securities Rulemaking Board (<http://emma.msrb.org>).

Prior to any bond transaction, with assistance from its financial advisors, remarketers, or underwriters, a marketing plan will be developed and outreach made to targeted investors (both existing and potential new investors). If necessary and/or desirable, in the view of MassDOT staff and its professional advisors, MassDOT will develop an internet roadshow and/or conduct an investor call in connection with a transaction.

MassDOT will respond to requests from investors and potential investors as appropriate and in a manner consistent with applicable securities laws.

### **12. Use of Derivatives**

MassDOT will maintain an Interest Rate Swap Management Policy ("Swap Policy"). Use of derivatives must comply with the terms of the Swap Policy then in effect. The Swap Policy is reviewed by the Finance and Audit Committee and adopted by the Board. Bond counsel and MassDOT's swap advisor also will be consulted in the event MassDOT is considering entering into or amending any swap or other derivative or hedging transaction.

### **13. Post-sale Monitoring, Management, Compliance**

MassDOT will maintain an adequate system of internal controls to provide compliance with applicable laws, rules, regulations, and covenants associated with outstanding debt. Annual calendars will be maintained identifying due dates for key financial activities including, but not limited to schedules for debt service payments, certificates of revenue sufficiency, maintenance of insurance, evaluation of the condition of facilities and continuing disclosure commitments. MassDOT will also maintain compliance with arbitrage rebate requirements, completing all calculations, filings, and payments with the IRS.

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MassDOT management constantly monitors current debt coverage ratios and future debt coverage ratios to make sure they are in compliance with covenants stipulated in the Trust Agreement. The MHS ratios are as follows:

Net revenues for such Fiscal Year shall be at least equal to the greater of:

- (a) 1.20 times the Senior Net Debt Service in such Fiscal Year;
- (b) 1.15 times the Combined Net Debt Service (Senior Net Debt Service plus Subordinated Net Debt Service) for such Fiscal Year; and
- (c) 1.0 times the Combined Net Debt Service plus the Capital Reinvestment Requirement for the Fiscal Year, which is established by the annual budget.

Investments of bond proceeds and other funds held under the trust agreements will only be invested in accordance with the terms of such trust agreements. Where possible, MassDOT will seek to limit negative arbitrage and engage and consult with outside advisors and counsel to monitor and optimize investment returns and negative arbitrage exposure.

MassDOT will abide by all regulations promulgated under the Dodd-Frank and by the Commodity Futures Trading Commission, the State Finance and Governance Board of the Commonwealth, and other applicable government regulations as may be enacted during the period covered by this Debt Policy. MassDOT will secure professional advice from an independent financial advisor, which shall be a registered Municipal Advisor, as defined under Dodd-Frank and applicable regulations thereunder, and bond counsel to assist in the process of reviewing possible transactions and in structuring, documenting and pricing any particular transaction that MassDOT decides to execute and will seek appropriate advice from its independent financial advisor including any necessary documentation that MassDOT received fair value in any transaction as required by these regulations and industry best practices

### **14. Guidelines for Issuing Refunding Bonds**

MassDOT will consider advance and current refundings based on a comprehensive analysis including when the following thresholds are met:

- Aggregate present value savings of refunded bonds are at least 3%
- Present value savings of each individual bond maturity refunded of at least 2%

In addition to the criteria above, MassDOT will also consider the refunding efficiency of each refunded maturity, the value of the call option being forfeited based on the potential to refund bonds for greater savings in the future, and the opportunity cost of refunding the bonds. Refunding efficiency of a refunded bond is defined as the present value savings for that refunded bond divided by the sum of the present value savings and the negative arbitrage associated with that refunded bond.

MassDOT reserves the right to issue refunding bonds when the above conditions are not met, based on the discretion of the Secretary/Chief Executive Officer and Chief Financial Officer,

subject to prior approval by the MassDOT Board of Directors. Circumstances that may supersede the above requirements include the desire to modify legal provisions on existing bonds, reduction of administrative costs related to keeping certain maturities of an existing series outstanding, or other attempts to restructure debt within the framework of this Policy. In cases where the above minimum refunding thresholds are not met, the circumstances for which refunding bonds were issued will be appropriately documented for the Board.

#### **15. Continuing Disclosure and Other Debt-Related Reporting Requirements**

MassDOT will comply with the requirements of all of its continuing disclosure undertakings by filing annually its disclosure statement and audited financial statements with EMMA. Significant event filings will also be made as and when necessary. MassDOT will also consider additional voluntary filings with EMMA as circumstances warrant.

MassDOT will comply with the terms of its trust agreements relating to the submission of annual budgets, audited financials and other documents to the applicable trustee or others, including credit and liquidity providers and direct purchasers of any bonds.

MassDOT will comply with the terms of the Enabling Act and other applicable law in respect to the delivery of reports, budgets, certificates and other items to the legislature, the administration, the State Finance and Governance Board or any other applicable entities, as applicable.

#### **16. Board Review, Approval and Revision of the Policy**

This policy will be updated every two years, or more often as required by federal or Commonwealth of Massachusetts regulatory authorities, including review by the Finance and Audit Committee and approval by the Board.

#### **17. Availability of Policy to Public**

A copy of this policy will be posted on the MassDOT's website ([www.MassDOT.state.ma.us](http://www.MassDOT.state.ma.us)) and will be made available to any members of the public upon reasonable request.

Approved February 10, 2016 by MassDOT Board of Directors