



MASSACHUSETTS DEPARTMENT OF TRANSPORTATION

DEBT ISSUANCE AND MANAGEMENT POLICY

April 23, 2018

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 opportunities to achieve economic savings and/or reduce various risks with respect to its fixed rate and variable rate debt and administering 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 i) restructuring opportunities pursuant to the risk management guidelines outlined in Section 8 below and ii) 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 an 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”). No bonds remain outstanding under 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 revenues from the Accepted Metropolitan Highway System (as defined in the MHS Trust Agreement) are pledged under the MHS Trust Agreement 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 refinancing from time to time bonds issued prior to July 1, 2009 pursuant to chapter 81A and the financing obligations of the Massachusetts Turnpike Authority relating to the turnpike and the metropolitan highway system. 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 coterminous with the Governor, while the remaining six members will be appointed to four-year terms 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 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 as required to comply 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 that hedge the variable rate debt.

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 refinancing from time to time bonds issued prior to July 1, 2009, pursuant to chapter 81A and the financing obligations of the Massachusetts Turnpike Authority relating to the turnpike and the metropolitan highway system. 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 required 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 and restructuring 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 the replacement of credit or liquidity facilities pertaining to variable rate 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 and services as needed to assist in the management of debt through a 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 considerations, and other factors deemed appropriate by the Secretary/Chief Executive Officer and Chief Financial Officer.

Any refunding, restructuring, reissuance or amendment of outstanding bonds will first be reviewed by the Finance and Audit committee and authorized by the Board of Directors. The Board of Directors may delegate to MassDOT officers the authority to execute and deliver documents as required to manage its debt under this policy.

6. Method of Procurement

In accordance with its procurement procedures, MassDOT periodically issues competitive requests for qualifications/proposals or otherwise engages professional services including for bond counsel, rebate compliance, financial advisor, investment advisor, swap advisor, credit facilities, liquidity facilities, remarketing agents 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 fixed rate bond obligations, 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, derivatives, liquidity providers, 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 in order to create greater diversification of credit, counterparty, and renewal or replacement risk. The risks evaluated by MassDOT prior to each transaction related to its variable rate portfolio include:

- (i) *Counterparty Risk (concentration and credit)*. 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 diminish this risk. MassDOT therefore has diversified its variable rate structures accordingly.
- (ii) *Market Pricing Risk (renewal and rollover)*. 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 derivative agreements are hedging variable rate risk as efficiently as possible.

MassDOT, its financial advisor, and bond counsel will continually evaluate MassDOT's refunding opportunities, debt and derivative portfolio restructuring opportunities, liquidity positions, 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 \$1.786 billion. Bonds issued under the MHS Trust Agreement amortize through January 1, 2039. There are no bonds outstanding under the WT Trust Agreement.

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 accordance with what is 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). 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 advisor, 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, amending or terminating any swap or other derivative or hedging transaction.

13. Post-Issuance Compliance, 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 credit and liquidity facilities and continuing disclosure commitments. MassDOT will also maintain compliance with arbitrage rebate and other post-issuance tax compliance requirements, completing all calculations, filings, and payments with the IRS in a timely manner.

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.

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 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 Section 15B of the Securities Exchange Act, 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. MassDOT will seek appropriate advice from its independent financial advisor, including documentation that MassDOT received fair value in any transaction, as required by applicable 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 Debt 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 laws 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) and will be made available to any members of the public upon reasonable request.

Approved April 23, 2018 by MassDOT Board of Directors