MOODY'S INVESTORS SERVICE

New Issue: Moody's assigns Aa3 to Nassau County Sewer and Storm Water Fin. Auth, NY's $162.3M rev bonds; Outlook is stable

Global Credit Research - 30 Oct 2014

NASSAU COUNTY SEWER & STORM WATER FINANCE AUTHORITY, NY
Sewer Enterprise
NY

Moody's Rating

ISSUE		RATING
System Revenue Bonds, 2014 Series A		Aa3
Sale Amount	$160,885,000	
Expected Sale Date	11/06/14	
Rating Description	Revenue: Government Enterprise	
System Revenue Bonds, 2014 Series B (Federally Taxable)		Aa3
Sale Amount	$1,455,000	
Expected Sale Date	11/06/14	
Rating Description	Revenue: Government Enterprise	

Moody's Outlook STA

Opinion

NEW YORK, October 30, 2014 --Moody's Investors Service has assigned an initial Aa3 rating to the Nassau County Sewer and Storm Water Finance Authority, NY's $160.8 million System Revenue Bonds, 2014 Series A and $1.4 million System Revenue Bonds, 2014 Series B (Federally Taxable). The bonds are special obligations of the Authority secured by a gross revenue pledge as defined in the General Revenue Bond Resolution between the authority and the trustee. The outlook is stable. The county has covenanted to levy an assessment or impose a charge sufficient to pay debt service on the revenue bonds, the Authority's operating expenses, Nassau County's (A2 stable) Sewer and Storm Water GO bonds currently outstanding and for operating expenses of the county's Sewer and Storm Water Resources District. Proceeds from the current issue will finance approximately $38 million in new money capital projects as well as fully refund the Authority's only outstanding debt, the Series 2004B and 2008A bonds, for an estimated net present value savings of $5.3 million, or 4.1% of refunded principal. The authority will take a majority of the savings in fiscal 2015.

SUMMARY RATINGS RATIONALE

The Aa3 rating reflects satisfactory bondholder protection, strong coverage of debt service, a historically stable and predictable revenue source, and a manageable debt position.

The stable outlook is reflective of the Authority's large, built out service area with strong coverage levels that are expected to remain stable.

STRENGTHS

-Stable and predictable revenue source

-Large and wealthy suburban Metro New York tax base

CHALLENGES

-Declining assessed valuation

DETAILED CREDIT DISCUSSION

SATISFACTORY LEGAL PROVISIONS; FLOW OF FUNDS KEY TO RATING

The legal structure provides strong bondholder protection and is a key driver to the high rating level and the differential from the county's GO rating. The county has covenanted to maintain assessments to make sum sufficient coverage of all of the authority's debt service,the authority's operating expenses, county GO debt issued for the sewer and storm water projects, and to cover all expenses at the Sewer and Storm Water Resources District. In the new Revenue Bond Resolution for this issue, the additional bonds test has been increased to a minimum of two times coverage.

The new structure of the flow of funds outlined in the Revenue Bond Resolution improves the authority's credit strength. Each year, the county will set the levy sufficient to meet its covenant. The Towns of Hempstead (Aa1 stable), North Hempstead (Aa1 stable), and Oyster Bay (A3 stable), and the Cities of Glen Cove (Baa3 stable) and Long Beach (Baa3 positive) will collect all assessments on behalf of the authority and remit the revenue to the trustee for the payment of debt service. The county has guaranteed full collection of the assessments and any shortfall will be taken from the county's own operating property tax revenue collected by the towns and cities. The authority's only financial obligation is to pay debt service on its revenue bonds and for minimal operating costs - the operations and management of the system itself are the county's responsibility. After debt service and operating costs, the authority will transfer the remaining revenue to the county for the payment of GO debt and system operations.

The two notch rating differential from the county's GO is reflective of these strong legal requirements. The assessments represent a stable and predictable source of revenue for these bonds. It is highly unlikely that the county would not set a tax levy sufficient to pay for operations given that it would greatly impact property tax revenue for its own operations. In the event that the county did not set a tax rate sufficient to cover debt service, the authority could sue the county to implement a sufficient assessment level.

The legal documents give the county the authority to change to a charge structure at any time, which could potentially weaken the credit quality of the bonds. Historically, management has chosen to levy an assessment on properties within the county, which exempts non-profit institutions, like hospitals and universities, who are among the greatest users of the system. To capture that lost revenue, the county could move to a fee structure based on usage. In the event that it did change to this structure, potentially the county itself would collect and remit the money to the trustee. The county is unlikely to alter the current structure given its historical practices and the stability and predictability of revenue collection. The county has proposed charging user fees to tax-exempt properties and maintaining assessments on taxable properties, but this remains under a legal challenge.

Under the Nassau County Interim Finance Authority (NIFA, Aa1 stable) legislation, NIFA has oversight of the authority's operations; this legislation also eliminates the county or the authority's ability to file for bankruptcy during the period NIFA's bonds are outstanding, currently through November 2025. The authority is considered a "covered organization" under the NIFA legislation. The NIFA oversight also reduces the risk that the county will not meet its covenant requirements.

GROSS REVENUE PLEDGE; FLOW OF FUNDS RESULTS IN STRONG DEBT SERVICE COVERAGE

As noted above, the county sets the levy and the three towns and two cities collect the revenue and remit to the trustee on a first-in basis. Given the county's rate covenant, this results in very strong debt service coverage. Over the past five years, debt service coverage of authority bonds has averaged 7.6 times. Revenues have been stable and are expected to increase going forward. Management projects that coverage will increase to over ten times in 2015, the year the county will take the majority of the savings from the current refunding, before declining to more historical levels of around 7.0 times.

Despite a declining assessed valuation within the county over the past few years, the revenues have remained stable. County management has increased the assessment rate to counteract the drop in valuation, maintaining revenues. The county's tax base remains large, highly diversified and stable. The county executive's proposed 2015 budget includes a tax levy increase for 2015. The county is fiscally responsible for sewer operations and any shortfall in revenues would be borne by the county.

The rate covenant and the flow of funds result in a material amount of revenue transferred to the county after it has paid debt service. This excess revenues will be used to fund district operations and pay the GO debt service of the sewer system. In 2013, the transfer of funds (including paying the county GO debt service) was $116 million, approximately 4% of the county's overall revenue structure.

OVERALL DEBT BURDEN LOW; DEBT CAPACITY LIMITED

The authority is limited to total debt issuance of $350 million, reducing the likelihood of diluted coverage through significant additional debt service. After this issuance, the authority will have $162 million of debt outstanding and $128 million in remaining capacity.

OUTLOOK

The stable outlook is reflective of the Authority's large, built out service area with strong coverage levels that are expected to remain stable.

WHAT COULD MAKE THE RATING GO UP

-Improvement in county operations that result in strong liquidity and reserve levels

-Significant improvement in authority debt service coverage levels

WHAT COULD MAKE THE RATING GO DOWN

-Revenue declines resulting in lower coverage levels

-A change in revenue structure

Key Statistics:

Security: Gross Revenue Pledge

Current Revenue structure: Assessments levied by the county

Additional Bonds Test: 2x

Debt Service Reserve Fund: None

2013 debt service coverage: 7.68x

2014 budgeted debt service coverage: 7.62x

Post sale debt outstanding: $162M

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. The additional methodology used in this rating was US Public Finance Special Tax Methodology published in January 2014. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

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