S&P Global Ratings

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Summary:

Pennsylvania Intergovernmental Cooperation Authority; Miscellaneous Tax

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Long Term Rating	AAA/Stable	Affirmed

Rationale

S&P Global Ratings has affirmed its 'AAA' rating on Pennsylvania Intergovernmental Cooperation Authority's (PICA) series 2009 and 2010 special tax revenue bonds (City of Philadelphia Funding Program). The outlook is stable.

The bonds are secured by a first lien on a 1.5% wage tax levied on city residents and on the net profits earned in business, professions, and other activities conducted by Philadelphia residents. PICA was created in June 1991 to provide a financing vehicle to assist in resolving Philadelphia's fiscal crisis. By legislation, this portion of the tax was ceded by the city to PICA in June 1991. Philadelphia has no recourse to these taxes until PICA debt service needs, as well as indenture requirements for reserves, are fully funded; excess wage taxes then flow as surplus for general city purposes.

PICA bonds are eligible to be rated above the sovereign because we believe it can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), U.S. state and local governments are considered to have moderate sensitivity to country risk. The authority's wage tax revenues are the primary source of security on the bonds, the institutional framework in the U.S. is predictable with state and local governments having significant autonomy, independent treasury management, and no history of federal government intervention.

The rating reflects our view of:

- Enabling legislation that precludes (except for refundings) additional future debt issuance;
- What we consider strong, growing debt service coverage (DSC) that has been steadily improving in the past decade and stood at 6.8x in fiscal 2016;
- Our view of a closed lien with a decline in annual debt service costs.

Other rating factors include:

- A potentially economically sensitive revenue stream that has performed reasonably well over time, including during the great recession; and
- Philadelphia's employment base, which is projected to increase at a moderate pace over the medium-to-long term.

PICA's enabling legislation prohibited new money debt issuance after Dec. 31, 1996 other than refunding for debt service savings. The legislation does permit refunding issuance. The lack of future debt issuance, projections of a continued trend of wage tax growth over time, and declining debt service should result in coverage levels increasing steadily through the life of the debt through 2023 when debt is fully amortized.

Bond provisions are a strong feature, in our opinion. By statute, the revenue stream is insulated from the general operations of the city of Philadelphia. The bonds are secured by a 1.5% tax on the salaries, wages, commissions, and other compensation earned by Philadelphia residents and on the net profits earned in business, professions, and other activities conducted by them. The tax is collected by the city, as agent for the commonwealth of Pennsylvania Department of Revenue, and is deposited on the day of receipt into a special account separate from the city's funds, for remittance the following day to the commonwealth, and held by the state treasurer with the commonwealth's other funds.

Pursuant to authorizing legislation, the proceeds and amounts on deposit are, at all times, the sole property of PICA and are not subject to appropriation by Philadelphia or the Commonwealth of Pennsylvania. On direction of PICA, on a weekly basis, payments are made directly by the state treasurer to the trustee.

The flow of funds are to the debt service fund; the debt service reserve (DSR) fund; payment of interest rate exchange, cap, or floor agreements; and to PICA for expenses. Excess monies then flow to the city. The DSR is funded at maximum annual debt service (MADS) on the bonds. No additional bonds, other than refunding bonds, are permitted under the authorizing legislation. There are only two bond issues outstanding (series 2009 and 2010 refunding issues) totaling approximately $266.1 million as of June 30, 2016. The bonds fully amortize in 2023.

Historically, coverage levels of MADS requirements have been growing, ranging from 2.82x in 1999, to 4.70x in fiscal 2009, to 6.83x in fiscal 2016. Coverage levels have been increasing in the past decade or longer due to savings generated from previous refundings, a leveling of debt service, and growth in the wage tax due to overall improvement in Philadelphia's economy.

As far as 2009, wage tax was growing consistently, averaging an annual increase of over 2%. However, in 2012, it fell by a marginal 0.6% but DSC was still maintained at a strong 5.37x. In 2015 and 2016, it grew at a rate of 7.5% and 9.1%, respectively. According to the city's five-year projections, it is expected to increase annually by over 3% through 2022. However, even when assuming no growth in the wage tax over the remaining life of the bonds, DSC is projected to remain strong, continuing to support the rating and grow to 11.97x in fiscal 2021, reaching 19.36x by maturity.

We consider Philadelphia's economy adequate. The city, with an estimated population of 1.6 million, is in Philadelphia County in the Philadelphia-Camden-Wilmington metropolitan area, which we consider broad and diverse. It has a projected per capita effective buying income of 78.3% of the national level and per capita market value of $86,954. Overall, market value was stable over the past year at $136.3 billion in 2016. The county unemployment rate was 6.9% in 2015.

Philadelphia is the commonwealth's largest city and the nation's fifth-largest by population. Its economy centers mainly on health care and higher education, but we do not believe the existence of related institutions understate the city's wealth and incomes. Leading city employers include Albert Einstein Medical, Children's Hospital of Philadelphia, Southeastern Pennsylvania Transit Authority, and Comcast. Development throughout the city is significant with 48

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major projects totaling nearly $7.4 billion, as of June 2016.

Outlook

The stable outlook reflects what we view as strong coverage and declining amortization costs, which would provide a cushion should pledged revenue decline, coupled with PICA's statutory inability (excluding refunding bonds) to issue additional debt. While unlikely, loss of employment resulting in reduced pledged revenues could lower DSC and result in a lower rating.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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