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**Summary:**

## Indiana

### Indiana Finance Authority; Appropriations; General Obligation; Moral Obligation

**Primary Credit Analyst:**

Oscar Padilla, Farmers Branch (1) 214-871-1405; oscar.padilla@spglobal.com

**Secondary Contact:**

Cora Bruemmer, Chicago + 1 (312) 233 7099; cora.bruemmer@spglobal.com

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## Summary:

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## Indiana Finance Authority; Appropriations; General Obligation; Moral Obligation

### Credit Profile

US\$63.165 mil lse approp bnds VRD Sec (Indiana) (Stadium Proj) RMKTD ser 2005 A-5 dtd 10/16/2005 due 02/01/2035

*Long Term Rating* AA+/A-1+/Stable New

Indiana ICR

*Long Term Rating* AAA/Stable Affirmed

### Rating Action

S&P Global Ratings assigned its 'AA+/A-1+' rating to the Indiana Finance Authority's (IFA) series 2005A-5 lease appropriation bonds (the stadium project), supported by Indiana.

This rating action reflects the remarketing of the bonds following the conversion of the interest-rate mode to the daily rate from the index rate, and the addition of a standby bond purchase agreement (SBPA) provided by U.S. Bank N.A., effective July 29, 2020.

The long-term component of the rating reflects IFA's pledged lease obligations. The short-term component reflects our assessment of the new SBPA provided by U.S. Bank N.A.

The SBPA will cover principal and 37 days' interest at a maximum 12% annual rate for the purchase price of bonds that are not successfully remarketed. The SBPA provides coverage for the bonds during the daily and weekly interest-rate modes. If the bonds' mode is converted to the term- or flexible-rate modes, the available interest commitment could be increased with bank consent.

The SBPA is due to expire on July 28, 2023, unless extended, replaced or terminated prior to the date. The SBPA provider's obligations to purchase tendered bonds will automatically terminate should certain events of default set forth in the agreement occur. These events, which we consider consistent with our published criteria, include, but are not limited to, the lowering of the rating on the bonds--or any of IFA's other debt that is senior to, or on parity with, the bonds--below 'BBB-'.

At the same time, we affirmed our 'AAA' issuer credit rating (ICR) on Indiana, our 'AA+' rating on the state's appropriation debt, our 'AA' rating on the Indiana Bond Bank's (IBB) moral obligation debt, and our 'A-1+' short-term rating on the state's 2008A lease revenue bonds (stadium project) based on Indiana's self-liquidity. The outlook on all long-term ratings is stable.

## **Credit overview**

As the intensity of recessionary headwinds fluctuates, we believe Indiana's strong credit fundamentals hallmarked by strong budgetary reserves, financial oversight, and management will continue to help the state navigate through an increasingly difficult operating environment. S&P Global Economics forecasts that the economic toll stemming from the COVID-19 pandemic will be substantial globally and estimates U.S. GDP to contract 5% for the year. (See "The U.S. Faces A Longer And Slower Climb From The Bottom," published on June 25, 2020 on RatingsDirect). Reflecting the state's strong financial oversight and management, the State Budget Agency (SBA), in collaboration with the Office of Management and Budget (OMB), has instituted new policies requesting agencies limit outlays and work to leverage federal resources where applicable to ensure budgetary soundness for the remainder of the biennium. The action follows SBA's request to agencies in late March to maximize current fiscal-year reversions and to develop new spending plans for the now ended fiscal 2020. Subsequently, agencies were asked to cut their budgets 15%, while state universities were asked to cut 7% for fiscal 2021--the second half of the state's biennial budget.

Favorably, the state entered fiscal 2020 on a strong footing, including \$2.27 billion in budgetary reserves equal to 13.6% of fiscal year 2019's operating revenue. As reported by SBA, the state ended fiscal year 2020 with a deficit of approximately \$882 million or 5.3% of expenses. Total general revenue for the fiscal year came in \$1.4 billion or 8.4% short of estimates (based on December 2019) with the individual income tax collections accounting for about two-thirds (\$930.2 million) of the gap. Like all states that levy an income tax, Indiana shifted its filing date to July from April to coincide with the federal deadline. Given filings for the year reflect incomes earned from the preceding calendar year, we anticipate filings made in July will approach initially estimated levels, although next year's filings will reflect the considerable slide in economic conditions currently being experienced, which will likely be reflected in the state's updated revenue estimate. The state's largest revenue stream--sales and use taxes--were 2% lower than estimated or \$163 million for the fiscal year.

As the state closed out fiscal 2020, it drew its reserves down to \$1.4 billion, equal to 9% of total expenses. In our view, the state's reserves will continue to provide it with flexibility to manage through the current recessionary period in tandem with its call to agencies to reduce their budgets to align with current expectations of softer revenue collections within the foreseeable future. While resources made available through federal relief programs, including the Coronavirus, Aid, Relief, and Economic Security Act (CARES Act), will help offset the direct costs borne by the state to combat the pandemic, to the extent funds cannot replace foregone revenues the state will have to continue to effectively work to maintain fiscal balance and preserve its remaining reserves to close the biennium and develop its subsequent biennial budget.

We understand the state's revenue estimates for the remainder of the biennium will be revised in September. With the governor's approval, the state budget director can withhold allotments of appropriations to agencies, if revenues are less than anticipated to prevent a deficit. Budget adjustments have historically been implemented regularly and on a timely basis. In our opinion, the state's government framework is significantly stronger than those of most states, reflecting our assessment of its relative flexibility to deal with changing fiscal positions or its ability to make necessary changes in a practical sense. (For additional information, see "When The Cycle Turns: Government Framework Is A Significant Factor In States' Ability To Navigate Downturns," published May 23, 2019).

A key credit consideration for the state's economic outlook will be the path its manufacturing sector follows through

this contractionary period. The sector has a comparatively large presence in the state and accounts for about 17% of its employment base. Should weakened demand for manufactured goods be prolonged, the state's path out of the recession could be slower and weaken its overall credit metrics, including state GDP and personal income gains. Current economic challenges notwithstanding, we anticipate the state's debt and liability profile will remain manageable. In addition, outside of the immediate term, Indiana's relatively low cost of living and business-friendly legislation and regulatory practices will, in our opinion, continue to make it an attractive target for firms looking to expand and relocate their operations.

The bonds are special, limited obligations of the IFA, payable solely from, and secured by, a pledge of the trustee of the trust estate in accordance with an amended and restated trust indenture dated May 1, 2015. The trust estate includes payments made by the Indiana Stadium and Convention Building Authority in accordance with the promissory note; all money obligated to be paid, according to the revenue deposit agreement, the lease, and the sublease. Lease-rental payments are payable from money appropriated by the general assembly at the request of the OMB on a biennial basis, and rental payments received by OMB from the Capital Improvement Board of Marion County pursuant to the sublease. We rate these bonds based on the state's appropriation pledge, which we rate one notch lower than the state's general creditworthiness, reflecting the appropriation risk associated with the annual payment. We believe these obligations provide funding for projects that we believe are significant to the state. Indiana also has an established track record of appropriating for resources necessary to satisfy debt service. In our opinion, there is no unusual political, timing, or administrative risk related to the debt payment. The bonds are on parity with the series 2005 A-1, 2005 A-4, 2007A-2, 2008A, and 2015A stadium project bonds.

We rate Indiana's other appropriation debt one notch lower than the state's general creditworthiness to reflect the appropriation risk associated with the annual payment. Our rating on the state's moral obligation debt is two notches lower than the state's general creditworthiness.

The ICR reflects our opinion of the state's:

- Maintenance of strong budgetary reserves, which have grown in each of the past three fiscal years;
- Active budget management, with practices that have been consistently applied to maintain sound reserve levels, including the administration's willingness to use its power to align appropriations with conservative revenue estimates and implement a lower cost structure;
- Modest economic growth across sectors, albeit at a modestly slower pace than the nation as a whole in recent years; and
- Low overall debt levels, but with significant contingent liabilities tied to infrastructure investment projects that could result in higher debt levels if toll revenues fall short of expectations.

The stable outlook reflects our view of Indiana's strong financial position and management's commitment to maintaining structural balance and a high level of reserves. In addition, we expect the state to make adjustments as necessary to try to maintain budgetary balance as revenues contract during this recession. We believe Indiana has demonstrated a strong commitment to strengthening budget and management controls and overall financial management, and we base our outlook on the expectation that these practices will continue to guide executive and

legislative actions.

### **Environmental, social, and governance factors**

Absent the implications of COVID-19, we consider the state's social risks to be in line with those of the sector, although the state's aging population and limited population growth will likely weigh on its demographic profile longer term. We view the state's governance and environmental risks as being in line with the sector. Indiana has historically maintained a strong management and policy framework to respond to developing risks.

## **Stable Outlook**

### **Downside scenario**

Should the current economic environment be prolonged and stress the state's operating framework to the point that active budget management proves insufficient to align revenues and expenditures, we would likely lower the rating. While we anticipate the state's economic metrics remaining below national levels, should the gap widen and be sustained, we could also lower the rating. We believe the state's pension liabilities remain manageable within the short-to-medium term, but its liability associated with its pay-as-you-go plan (Pre-1996) could add budgetary and credit pressure as resources in its pension stabilization fund are exhausted and appropriations fund annual contributions in their entirety.

## **Credit Opinion**

For the foreseeable future, restrained and restricted economic activities resulting from the COVID-19 pandemic will translate directly into contracted economic output and general revenue declines as demonstrated in the final quarter of the state's fiscal 2020. While we anticipate the current situation will remain fluid, the state's active management will remain a key credit consideration in addressing developments on the ground and the subsequent second-order effects as they materialize. Prior to the onset of the pandemic, the state was in step with the national economic expansion, which had lasted over a decade.

According to Bureau of Economic Analysis (BEA), Indiana's economy grew a modest 0.8% in 2019, trailing the national level of 2.3%. The state's durable goods manufacturing sector was a drag on its overall growth, contributing negative 0.18 percentage points to the state's GDP in 2019, according to BEA. The sector accounts for about 17% of the state's total employment and although it experienced a relatively strong 2017 and 2018, it softened throughout 2019. Of note, IHS Markit estimates manufacturing employment will contract 9.5% and 3.6% in 2020 and 2021, respectively, which, in our view, will add to economic weakness, particularly in the northeastern and south-central regions of the state, which have high concentrations of manufacturing employment. The sector's sluggishness, which, even prior to the pandemic reflected weaker foreign demand growth and trade uncertainties, will, in our view, weigh on the potential growth prospects and limit the pace of economic recovery outside the short term. The state has nevertheless been responsive to changing economic trends, in our view, evidenced by growth in professional and business services, transportation and utilities, and education and health services. In our opinion, Indiana's relatively low cost of living and business-friendly legislation and regulatory practices will continue to make it an attractive target for firms looking to expand and relocate their operations as economic conditions improve. Furthermore, the state

capital, Indianapolis, offers a highly diverse economy with several sectors that should see a healthy return to growth as pandemic challenges abate.

While the state's economic growth lagged that of the nation in 2019, its general fund achieved a \$410.5 million operating surplus (as reflected in the state's surplus statement). Including other expenditures and transfers and reversions, the state's general fund balance totaled \$834.5 million, up from \$366.4 million. Its combined reserve balances totaled \$2.27 billion, or nearly 14% of total appropriations for the year.

On a generally accepted accounting principles (GAAP) basis, Indiana's assigned and unassigned available general fund balance at fiscal year-end June 30, 2019, was approximately \$3.67 billion, or approximately 23% of general fund expenditures and net transfers, up \$36.64 million from the year before.

The state's enacted 2020-2021 biennial general fund budget totaled \$34.59 billion with fiscal 2021 totaling \$17.49 billion, before adjustments or reversions. Given the call to achieve savings and cuts, we anticipate the state's expenditures for the year will decrease although an estimate is not available at this time. Appropriations for public education and health and human services account for a little over 86% of total general fund appropriations. When adopted the structurally balanced budget fully funded pension obligations and Medicaid growth, which has not changed. In our view, Indiana's demonstrated commitment to maintaining structural balance while also addressing its long-term liabilities is a credit strength.

The state constitution does not allow new debt except to meet casual deficits in revenue, pay interest on state debt, or provide funds for public defense. Therefore, Indiana has no general obligation (GO) or tax-supported revenue debt, but the state does have appropriation-backed debt. Its debt levels are low, in our view, at approximately \$258 per capita and 0.5% of personal income and gross state product (GSP), respectively. Debt service accounted for about 1.4% of the state's governmental fund expenditures (less federally funded expenditures) in the past three fiscal years, which we consider low. Amortization is rapid, with nearly 75% retired over 10 years. Tax-supported debt outstanding totals about \$1.87 billion, which accounts for self-supported debt of approximately \$900 million (IFA stadium and convention center). We currently do not include bond bank debt that is secured by the state's moral obligation pledge, which totaled approximately \$145 million (as of June 30, 2019). In addition, while Indiana has appropriated for the university fee-replacement debt in the past, there is no appropriation pledge supporting the bonds and the state is not obligated to appropriate for it in the future. Therefore, we do not include the university fee-replacement debt in Indiana's debt calculation. Our calculated total includes the net present value of final acceptance payments of approximately \$512 million related to the state's East End Crossing P3 project.

Indiana's unfunded pension liability represents its proportionate share in several pension plans, of which the Teachers Retirement Fund (TRF Pre-1996) and the Public Employees Retirement Fund (PERF) are the largest. The Indiana State Teachers' Retirement Fund consists of the closed pre-1996 account and the new 1996 account. In 1996, Indiana closed the plan and moved new hires to actuarially sound plans. The new plan, which is the responsibility of school districts, includes transferred teachers from the state plan. The state funds the closed pre-1996 account on a pay-as-you-go basis and the fund was approximately 25.7% funded as of June 30, 2019, as expressed by the fiduciary net position as a percent of the total pension liability. The total pension liability was \$14.39 billion with a total fiduciary net position of \$3.7 billion, leaving a net pension liability of \$10.69 billion. The PERF's pension funded ratio was 79.4% with a net

pension liability of approximately \$3.4 billion, of which state's proportionate share was approximately \$868 million. As part of its plan to address the significant unfunded liability, Indiana also adopted a 30-year amortization schedule and established a pension stabilization fund, which should limit the annual growth rate of general appropriations for the TRF Pre-1996 to less-than-historical general revenue growth rates. The pension stabilization fund is a dedicated fund in the TRF Pre-1996, designed to accumulate a balance during a 12-year period. The fund is allowed to smooth out yearly general fund contribution growth to less than 3%; the original statute allowed use of the fund to start in 2007.

The overall average pension funded ratio over the previous three years was 63%, which we view as relatively low and far removed from what we consider good levels (80%). In our opinion, while our calculated pension funding ratio is relatively low, our holistic assessment captures the relative weight and risk associated with the state's pre-1996 plan, which represents three-fourths of the total accrued liability. Given that it is structured as a pay-as-you-go plan, appropriations will fund actuarially determined contributions (ADCs) in their entirety when they equal the expected benefit payment. Peak appropriations are projected to occur in 2026. To the extent that we believe the state will continue to support all its plans, the relative risk within the short-to-medium term is manageable, in our view. Our assessment also captures the relatively well-funded status of the state's other plans, which in aggregate are weighed down by the pre-1996 plan. The state has been contributing 100% of its ADCs to its systems and statutory (pay-as-you-go) requirement for the TRF Pre-1996 plan. The five-year average rate of return for PERF is 5.1%, which is below the assumed rate of return of 6.75%, although not significantly so, in our view. On the whole, management factors and actuarial inputs do not significantly encumber or improve our view of the state's overall pension funding discipline.

In terms of other postemployment benefits (OPEBs), the net liability was a manageable \$124.87 million, or slightly less than \$20 per capita. The decline in the state's OPEB liability stems from changes to benefit terms of the Indiana Police OPEB plan, which reduced its liability to \$198.44 million from \$324.51 million. The state is currently funding the OPEB liability on a pay-as-you-go basis.

Indiana's bonds are eligible to be rated above the sovereign, because we believe the state can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013), U.S. states are considered to have moderate sensitivity to country risk. State-derived revenues are the sole source of security on the bonds, and the institutional framework in the U.S. is predictable, with significant state autonomy and flexibility.

For more information, see the full analysis on Indiana, published April 28, 2020.

Based on the analytic factors we evaluate for states, on a scale of '1.0' (strongest) to '4.0' (weakest), we have assigned a composite score of '1.6' to Indiana, which equates to an indicative rating score of 'AA+'; however, we have applied our one-notch up flexibility as per our state methodology criteria. The 'AAA' ICR on Indiana reflects our view of the state's proven commitment to and significant focus on strengthening the budget through extensive use of management controls that have led to maintenance of structural balance, growth in reserves, and continued funding of long-term liabilities.

## Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of July 22, 2020)		
Indiana Bnd Bank (Adams Cnty Memorial Hosp Proj) MORALOB		
<i>Long Term Rating</i>	AA/Stable	Affirmed
<b>Indiana Bnd Bank, Indiana</b>		
Indiana		
Indiana Bnd Bank (Indiana) MORALOB		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (AGM)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (AGM)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (AMBAC)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (MBIA) (National)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
<b>Indiana Finance Authority, Indiana</b>		
Indiana		
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/A-1/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		



Ratings Detail (As Of July 22, 2020) (cont.)		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
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Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/A-1/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) (Stadium Proj) ser 2005 A-4		
Unenhanced Rating	NR(SPUR)	
Indiana Fin Auth (Indiana) (Stadium Proj) ser 2005 A-5		
Unenhanced Rating	NR(SPUR)	
Indiana Fin Auth (Indiana) (Stadium Proj) 2007 ser A-2		

Ratings Detail (As Of July 22, 2020) (cont.)		
<i>Long Term Rating</i>	AA+/A-1/Stable	Affirmed
<i>Unenhanced Rating</i>	NR(SPUR)/NR	
Indiana Fin Auth (Indiana) (Stadium Proj) 2007 ser A-3		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
<i>Unenhanced Rating</i>	NR(SPUR)	
<b>Indiana St Office Bldg Comm, Indiana</b>		
Indiana		
Indiana St Office Bldg Comm (Indiana) APPROP		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Indiana St Office Bldg Comm (Indiana) APPROP		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Indiana St Office Bldg Comm (Indiana) APPROP (MBIA of Illinois)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
<b>Indiana Transp Fin Auth, Indiana</b>		
Indiana		
Indiana Transp Fin Auth (Indiana) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Indiana Transp Fin Auth (Indiana) APPROP (wrap of insured) (FGIC & AGM) (SEC MKT)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Indiana Transp Fin Auth (Indiana) APPROP (FGIC) (MBIA) (National)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Indiana Transp Fin Auth (Indiana) APPROP (FGIC) (MBIA) (National)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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