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Fitch to Include Disclosure on PR Special Rev Ruling in Related Issuer Research.

Fitch Ratings-New York-09 March 2018: On March 12, 2018 Fitch Ratings will begin inserting a comment into its rating action commentaries (RACs) for credits the agency believes could be affected if a final ruling upholds a recent decision on the interpretation of a section of Chapter 9 of the U.S. bankruptcy code. A Jan. 30, 2018 district court ruling dismissed claims regarding payment of Puerto Rico Highways and Transportation Authority (PRHTA) debt. The ruling states that section 922(d) was included in the code as permission for a municipality to continue paying special revenue obligations if it chooses to do so during bankruptcy rather than as relief for bondholders from the constraints of the code's automatic stay provisions.

A final ruling in the case that is consistent with this approach would create uncertainty about full and timely payment of special revenue obligations including those of utilities, transportation, and other enterprises of local governments as well as some dedicated tax bonds in the event the related government files for a Chapter 9 bankruptcy. Fitch's Rating Criteria for Public Sector, Revenue-Supported Debt already consider the influence on enterprise debt of the credit quality of the general government, including common management and service area characteristics as well as legal, financial and operational connections. Restrictions on the use of pledged revenues for other municipal purposes, such as federal law prohibiting diversion of airport revenues to other municipal uses, is another strong credit consideration.

Fitch will insert the following comment in RACs it believes are subject to uncertainty in the event of a final ruling in the PRHTA case that is consistent with the district court ruling:

"A Jan. 30, 2018 district court ruling that dismissed claims regarding payment of Puerto Rico Highways and Transportation Authority debt has raised questions about the scope of protections provided by Chapter 9 to bonds secured by pledged special revenues. Fitch's rating criteria treat special revenue obligations as independent from the related municipality's general credit quality. The outcome of the litigation could result in modifications to Fitch's approach. For more information, see 'What Investors Want to Know: The Impact of the Puerto Rico Ruling on Special Revenue Debt' (February 2018)."

Fitch will not include this comment in RACs of bonds rated based on the pledged special revenue definition described in section 902(2)(E) of the code. In these cases, Fitch believes the possibility of a payment interruption due to an automatic stay would remain remote even if the recent ruling were to stand. Fitch sets a high bar to consider tax-supported debt to be secured by pledged special revenues under section 902(2)(E) and thus unaffected by the operating risk of the related municipality. Among the elements required for Fitch to rate such bonds without regard to the government's issuer rating is a statutory requirement that a governmental official outside the municipality collects and remits the tax revenues to the paying agent, placing the funds outside the control and direction of the municipality.

Fitch has most commonly applied this analysis to bonds issued by school districts in California. In

Fitch’s opinion, this structure places the bond security outside the scope of the Puerto Rico decision. The court’s opinion notes that section 922(d) permits third parties to continue to apply special revenues held by them to debtors, free from the automatic stay.

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