

**Fiscal Year 2011 Report on Debt Management
To the
Public Finance Management Board**

September 2012

**State of Rhode Island
And Providence Plantations**

OFFICE OF THE GENERAL TREASURER

***GINA M. RAIMONDO
GENERAL TREASURER***

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State of Rhode Island and Providence Plantations
Office of the General Treasurer

Gina M. Raimondo
General Treasurer

September 2012

Members of the Rhode Island Public Finance Management Board

Mr. Richard Licht, Director of Administration, State of Rhode Island
The Honorable A. Ralph Mollis, Secretary of State, State of Rhode Island
Mr. W. Lincoln Mossop, Jr., Public Member
Mr. Robert A. Mancini, Public Member
Mr. Edward F. Yazbak, Public Member
Mr. Steven Filippi, Public Member
Mr. Thomas M. Bruce, III, Public Member

Dear Members of the Board:

I hereby submit the fiscal year 2011 Debt Management Report for the State of Rhode Island and Providence Plantations (the "State" or "Rhode Island"). This report once again demonstrates the continued importance of closely monitoring the State's debt management efforts to maintain and improve the State's credit worthiness.

In recent years, debt management has been a top priority of the State resulting in significant improvement in several long-term debt trends. As recently as 2001, Rhode Island's debt burden was the 7th highest nationally according to Moody's Investors Service. The 2011 Moody's State Debt Medians show that Rhode Island's ranking has dropped to 12th for debt per capita and 14th for debt as a percentage of personal income.

Net tax supported debt totaled \$1.76 billion at the close of FY 2011 and current Budget Office forecasts project the State's debt level to increase slightly to \$1.77 billion by FY 2016.

A major responsibility of the Treasurer's Office and the PFMB is to monitor State debt ratios and to preserve and enhance Rhode Island's credit ratings and presence in the financial markets. Maintenance of prudent debt ratios and securing positive ratings from the credit rating agencies will allow Rhode Island to obtain financing at the lowest possible interest rates. To maintain its credit ratings at an appropriate level, the State must continue to make fiscal responsibility a top priority.

Rhode Island's fiscal situation was characterized as "strained" by the three major credit rating agencies prior to the national recession. The economic downturn and the global financial crisis had a serious impact on the financial flexibility of all the states that was felt for several fiscal years.

The State's credit rating agencies highly scrutinized budgetary decisions during this challenging time. Maintenance of the State's "Double A" category ratings is more important now than ever before, as credit spreads reached their widest levels in decades in 2008 and have remained above historical levels. The ability to access the capital markets has become increasingly challenging for issuers such as the State. The demise of the municipal bond insurance industry, coupled with the credit squeeze and the notable absence of several major investment banking firms will continue to have an impact on the State as it seeks to finance its capital needs. Navigating these elements will be a significant priority for the State to insure continued access to capital at affordable levels.

According to State Budget Office projections, it appears that the ratio of debt service to revenues will remain within the PFMB's guideline of 7.5%. The economic climate of the past three fiscal years has resulted in anemic revenue growth. Since the State must continue to issue debt to fund its capital needs, the increased debt service is a growing percentage of a smaller revenue base. At this time, we do not recommend revision of the guideline, but careful monitoring as noted above.

Sincerely,

A handwritten signature in black ink, appearing to read "Gina M. Raimondo", written in a cursive style.

Gina M. Raimondo
General Treasurer

SECTION 1

2011 Findings

The 2011 Report includes the following:

- Φ Analysis of current State debt position and trends.
- Φ Status report on the implementation of debt management methods and policies.
- Φ Evaluation of projected new debt issuance in compliance with the Public Finance Management Board's ("PFMB") adopted Credit Guidelines.
- Φ Information about outstanding debt issued by State-related agencies and summary information on local government debt position and trends.

The principal findings of this report are summarized below.

Rhode Island's Debt Burden Remains Moderately High

Rhode Island's debt levels continue to improve, but are still relatively high, as evidenced by the following statistics provided by a Moody's Investor Service State Debt Medians Report, May 2012 and the FY13 Capital Budget:

- Rhode Island ranks 14th highest among all states in Net Tax-Supported Debt as a percent of personal income, at 4.7% (based on Moody's calculations and 2010 personal income).
- Rhode Island ranks 12th highest among all states in Net Tax-Supported Debt per capita at \$1,997 (based on Moody's calculations).
- Net Tax-Supported Debt increased annually by 2.1% from FY07 – FY11. Personal income growth for the same period was 2.0%.
- In FY11 the general obligation debt decreased at a rate of 6.1% over FY10. From FY07 – FY11 general obligation debt increased at a rate of 3.5%.

Over the last four years, Net Tax-Supported Debt increased by \$138.0 million, from \$1.62 billion at FY07 to \$1.76 billion at FY11. Current Tax-Supported Debt of \$1.76 billion represents a decrease of 6.6% from \$1.88 billion at FY10.

According to the FY13 Capital Budget, the State's outstanding Net Tax-Supported Debt (includes adjustment for agency payments) is projected to remain stable at \$1.77 billion for FY16. This projection assumes the issuance of no new Tax Supported Debt during this period other than as projected in the Capital Budget.

The Capital Budget for FY13 also indicates that State general obligation debt will decrease at a compound annual growth rate of 0.4% from \$1,119.4 million at FY12 to \$1,103.8 million at FY16. The Economic Development Corporation debt will increase at a compound annual growth rate of 3.6%. During the same period, it is estimated that capital leases will decrease at a compound annual growth rate of 9.8% and Convention Center Authority will decrease by 4.4%.

Rhode Island's efforts to improve its debt position continue to be recognized by the municipal credit rating agencies. Pension reform measures that were adopted during the 2005 legislative session contributed to Standard and Poor's upgrade of the State's bond rating from AA- to AA. Protecting the gains made in debt reduction is critical and important to preserving financial flexibility.

In 2010 two of the municipal rating agencies recalibrated municipal ratings. Fitch completed their process in April 2010 and Moody's recalibrated the states in May 2010. Standard & Poor's had been using one rating scale for approximately two years. These actions were in response to the Markets' demand for enhanced comparability between municipal ratings and non-municipal ratings. As a result of recalibration, the General Obligation ratings of the States are higher on the "global" or "corporate" scale than their place on the municipal ratings scale. However, these actions were not viewed as improvements in credit quality or rating upgrades, but as an alignment of municipal ratings with corporate or global equivalents.

In a Special Comment publication dated July 22, 2010, Moody's Investors Service noted that the key drivers of state government credit quality in the near term are;

- Reliability of budgets
- Revenue forecasts
- Risk of double dip recession
- Magnitude of structural imbalance
- Phase-out of federal stimulus (ARRA) funding
- Financial flexibility and availability of reserves
- Available liquidity
- Extent of long-term liabilities
- Exposure to variable rate debt
- Political consensus related to spending and benefit levels

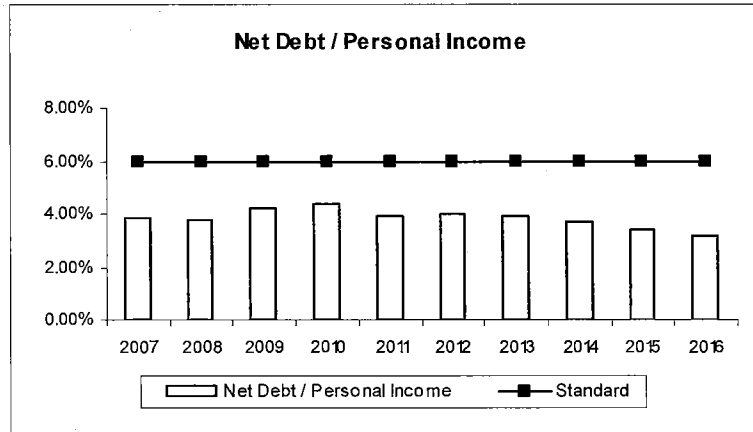
PFMB's Credit Guidelines and Debt Ratio Targets

In recognition of Rhode Island's high debt burden, the PFMB adopted Credit Guidelines recommended in the 1997 report for use in evaluating certain elements of the State's debt. The original Credit Guidelines were adopted after extensive research on State debt trends and a comparative analysis of certain "peer" states with demographic, geographic, and financial characteristics similar to Rhode Island. The Credit Guidelines were intended to be restrictive enough to be relevant in managing debt levels, but flexible enough to allow for the funding of critical infrastructure needs. However, in light of the State's already high debt burden at the time of adoption, the Credit Guidelines did not necessarily represent an "ideal" level of State debt.

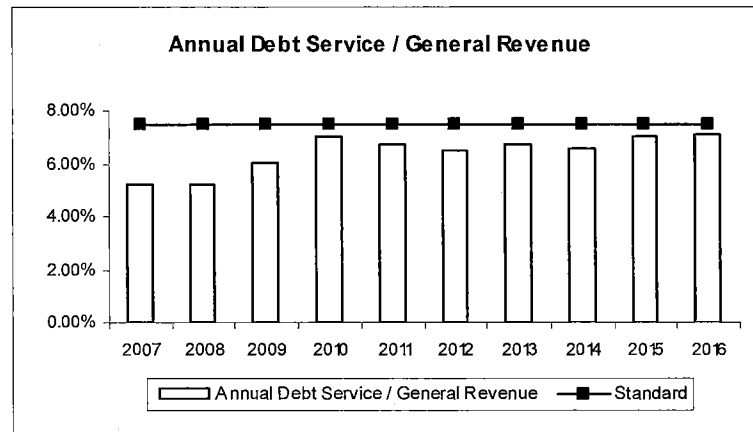
The PFMB approved the following revisions to the Tax-Supported Debt to Personal Income target debt ratios recommended in the 1999 Report on Debt Management. Approved guidelines are as follows:

- ***Credit Guideline 1:*** Tax-Supported Debt to not exceed the target range of 5.0% to 6.0% of personal income, and annual debt service for Tax-Supported Debt to not exceed 7.5% of General Revenues. It is anticipated that fluctuation of this ratio over the long-term will be affected by both variations in personal income levels and debt issuance. The target ranges will continue to be reviewed on an annual basis with consideration given to trends in the State's debt level and upcoming infrastructure projects.
- ***Credit Guideline 2:*** The Board should monitor the total amount of Tax-Supported Debt, State Supported Revenue Debt, and Agency Revenue Debt in relation to the State's personal income.
- ***Credit Guideline 3:*** The Credit Guidelines may be exceeded temporarily under certain extraordinary conditions. If a Credit Guideline is exceeded due to economic or financial circumstances, the Board should request that the Governor and the Legislature recommend a plan to return debt levels to the Guidelines within five years.

The debt projections in this report remain within the Credit Guidelines relating to Net Debt to Personal Income, as the ratio will decline from 4.0% at FY12 to 3.2% at FY16. From FY07 to FY11, Personal Income grew at a rate of 2.0%, while Net Tax-Supported Debt increased by 2.1%. The combination of lower Personal Income growth and lower debt growth resulted in the Net Debt to Personal Income ratio of 3.9% at FY07 remaining stable at 3.9% for FY11.



Annual Debt Service as a percentage of revenues increased from 5.2% in FY07 to 6.7% in FY11. Projections from FY12 to FY16 indicate compliance with the PFMB's guidelines as the FY12 - FY16 debt service to revenues ratio does not exceed 7.5%.

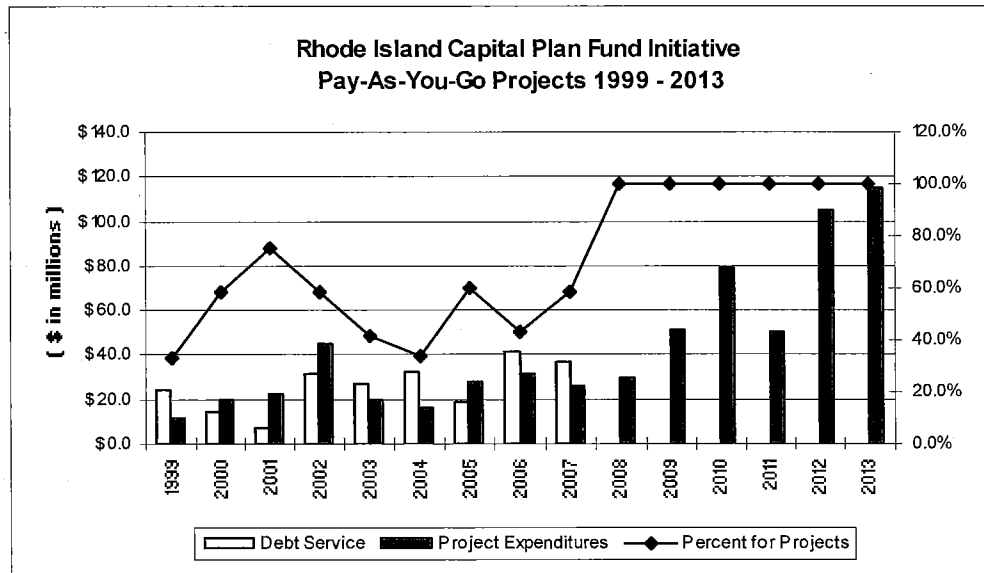


Positive Steps in Debt Administration

Over the years, Rhode Island has made improvements to its debt planning and administration, beginning with the implementation of a formal capital budgeting process and the adoption of the Public Corporation Debt Management Act in 1994 (§RIGL 35-18). The State’s debt load can have a negative impact on the flexibility of the operating budget and limits the State’s ability to meet unanticipated capital financing and economic development needs. Listed below are several initiatives related to debt administration undertaken by the State in recent years.

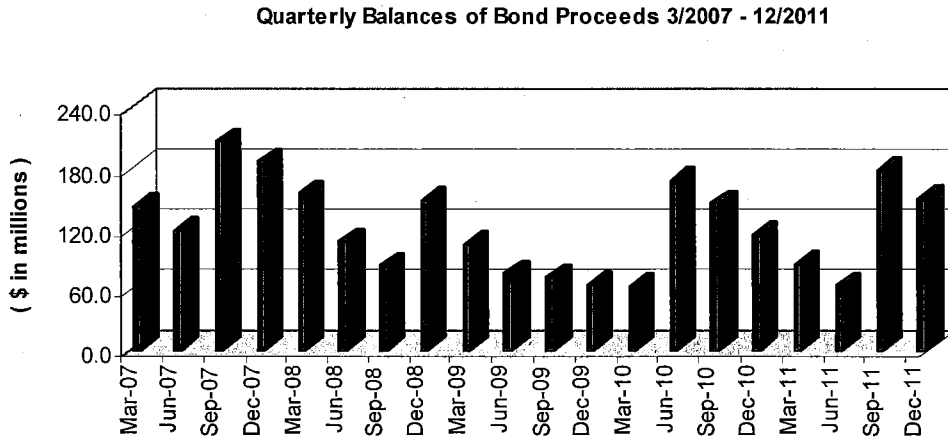
1. **Pay-As-You-Go Capital Financing.** During a period of sustained economic expansion from 1998 – 2001, along with improved cash management, the State was able to forego cash flow borrowing, a positive trend in the State’s debt management. However, economic conditions compelled the State to borrow on a short-term basis in 2002, 2003 and 2006 thru 2011. Greater financial flexibility during periods of economic expansion enabled the State to increase the proportion of pay-as-you-go capital spending, which includes using both gas tax funds and funds dedicated to the Rhode Island Capital Fund. [UPDATE ON RICAP]

Included in the governor’s recommended FY13 Budget was a \$115.3 million appropriation (\$105.0 million in FY12 which includes funding reappropriations from FY11) for pay-as-you-go capital financing through the Rhode Island Capital Plan Fund. According to the FY13 Capital Budget, 100.0% of the Fund’s resources will be used for capital asset protection projects in FY13.

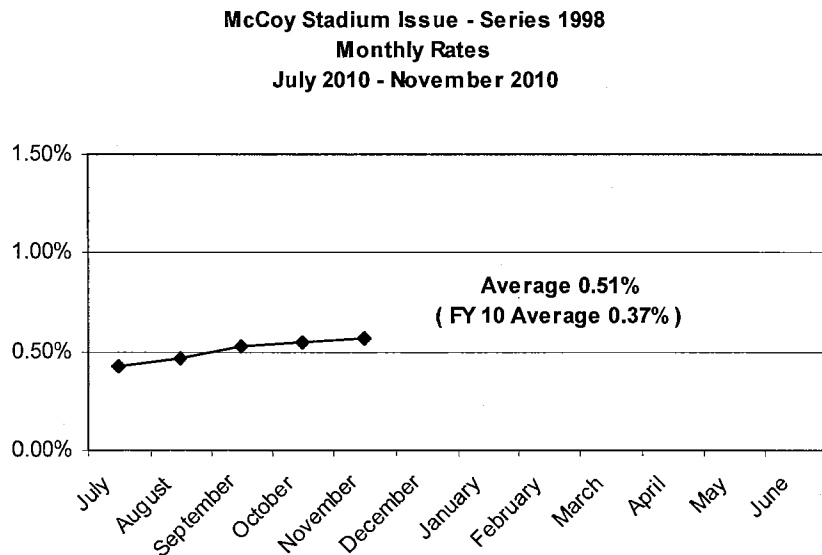


2. Bond Proceeds Management. The State continues to monitor the issue of unexpended balances of general obligation bond proceeds. Past reports have noted this as an issue of concern. Unexpended proceeds were \$151.1 million as of December 31, 2011 up from \$114.8 million as of December 31, 2010.

As shown in the chart below, there is a cyclical peak at the end of the second or third quarter, which is indicative of the traditional timing of bond issuance.



3. Variable Rate Debt Obligations Issued. The State was involved in a variable rate financing for McCoy Stadium that was issued by the Economic Development Corporation in July 1998. The floating rate structure offered (1) low initial interest rates, (2) principal structuring flexibility, including prepayment without penalty, and (3) the ability to convert to a fixed rate on one month's notice. The State also issued two series of variable rate bonds in the 1990's that were subsequently refunded by fixed rate bonds. At the time of issuance, the variable rate component improved the match of State assets and liabilities and provided a lower overall cost of capital.



The General Treasurer and the State Budget Office have implemented a policy which restricts the total amount of variable rate exposure to 10% of net tax supported debt outstanding.

In the 2001 session of the RI General Assembly, the Legislature approved a bill proposed by the Treasurer's office to permit the State to enter into interest rate swap agreements with the goal of reducing borrowing costs. This effectively permits the State to convert a fixed rate obligation to a variable rate obligation or vice-versa. The fiscal impact of future transactions is not possible to quantify since any benefit derived from the use of variable rate debt and related interest rate swaps is extremely dependent upon market conditions, the extent to which the investment vehicle is utilized and the specifics of the individual transaction. The State can only enter into such transactions when there are demonstrated savings. To date the State has not utilized interest rate swaps but has provided assistance to various state agencies in analyzing financing alternatives, refinancing variable rate debt and unwinding swaps. The final installment on the McCoy Stadium bonds was made on December 15, 2010, eliminating any State exposure to variable rate debt.

4. **Municipal Debt Report.** The PFMB is also required to report on R.I. local government debt which is a summary of debt issued by cities and towns and other authorities to comply with Section 42-10.1-4. This report will be issued on or before September 30, 2012.

SECTION 2

Rhode Island State Debt

Table 2-1 below is a summary detail statement of outstanding State debt, followed by a brief glossary of terms describing each category of debt.

Table 2-1								
Rhode Island Debt Statement								
(as of June 30, 2011, dollars in millions, principal amount)								
						<u>6/30/2009</u>	<u>6/30/2010</u>	<u>6/30/2011</u>
Tax-Supported Debt								
	General Obligation Bonds					\$ 1,036.2	\$ 1,118.0	\$ 1,049.4
	Capital Leases					267.1	254.7	233.6
	Convention Center Authority					263.8	268.3	259.6
	Economic Development Corporation					286.5	259.9	238.4
	R.I.H.M.F.C. Neighborhood Opportunities Housing Program					13.2	8.4	3.5
	Refunding Bond Authority					6.0	-	-
	Gross Tax-Supported Debt					\$ 1,872.8	\$ 1,909.3	\$ 1,784.5
	Agency Payments					(26.6)	(25.4)	(24.1)
	Net Tax-Supported Debt					\$ 1,846.2	\$ 1,883.9	\$ 1,760.4
State Supported Revenue Debt								
	EDC - Providence Place Mall					30.4	28.6	26.7
	R.I. Housing					285.3	267.3	235.2
	Industrial Recreational Building Authority - Insured							
	Industrial Facilities Corporation					14.1	18.1	20.8
	State Supported Revenue Debt					\$ 329.8	\$ 314.0	\$ 282.7
Agency Revenue Debt								
	Airport Corporation					\$ 327.7	\$ 319.7	\$ 309.7
	Economic Development Corporation					94.4	94.0	97.5
	EDC - GARVEE Bonds, Federally Funded					427.4	400.5	372.3
	R.I. Housing					5.0	5.0	5.0
	Narragansett Bay Commission					444.0	410.1	422.4
	Resource Recovery Corporation					14.8	14.0	13.1
	State University and Colleges					222.6	283.1	276.2
	Turnpike and Bridge Authority					23.6	70.7	69.2
	Water Resources Board					5.8	4.9	4.1
	Agency Revenue Debt					\$ 1,565.3	\$ 1,602.0	\$ 1,569.5
Conduit Debt								
	Clean Water Finance Agency					\$ 602.6	\$ 652.7	\$ 671.2
	Health and Educational Building Corporation					2,377.6	1,793.7	2,574.5
	R.I. Housing					1,293.7	1,445.1	1,416.5
	Industrial Facilities Corporation					89.3	95.3	80.8
	Student Loan Authority					1,046.3	1,331.4	1,026.6
	Water Resources Board					1.0	-	-
	Conduit Debt					\$ 5,410.5	\$ 5,318.2	\$ 5,769.6
Sources: FY 13 Capital Budget and Treasury Survey of R.I. Quasi-Public Corporations.								

Explanation of Categories of Debt

Below is a definition of the four general categories of debt, which are used throughout this report and reflected in Table 2-1 on the previous page. These categories are listed in declining relationship to the State's general credit. To the extent possible, the categories are consistent with the methods credit analysts use in reviewing a state's debt levels. Credit analysts are the professionals who assign credit ratings and recommend and evaluate debt as investments for investors in tax exempt bonds.

Tax-Supported Debt

Tax-Supported Debt is payable from or secured by general taxes and revenues of the State or by specific State collected taxes that are pledged to pay a particular debt. Because of the claim this debt has on the State's credit, this is the most relevant debt figure to State taxpayers.

State Supported Revenue Debt

State Supported Revenue Debt is payable from specified revenues pledged for debt service which are not general taxes and revenues of the State. However, the State provides additional credit support to repay this debt if the pledged revenues are insufficient to meet scheduled debt service requirements. Because of the contingent nature of the State Credit Support, this figure is somewhat less important than Tax Supported Debt. This type of debt includes "moral obligation" debt.

Agency Revenue Debt

Agency Revenue Debt is similar to State Supported Revenue Debt; except that no State credit support is legally pledged for repayment and the assets financed are State owned enterprises that are intended to be supported by internally generated fees and revenues. While this type of debt is not supported by State taxes, the agencies and public corporations responsible for this debt may also have financed some assets with State general obligation debt, thereby indirectly linking such debt to the State.

Conduit Debt

Conduit Debt is issued by a state agency or public corporation on behalf of borrowers which include businesses, health care institutions, private higher education institutions, local governments, and qualified individuals (loans for higher education and housing purposes). No State credit support is provided.

SECTION 3

Classification of State Debt

The Debt Issuers

The electorate of the State and the General Assembly authorize certain State officers, State agencies, and municipalities to issue debt for various purposes. This report uses the terms “issuers” and “debt issuing agencies” to describe any State office, department, corporation, or agency which issues bonds, notes, or other securities. These issuers finance construction and other capital improvements to State buildings; State highways; local water, sewer, and other capital improvement projects; loans to businesses; health care organizations; loans to low and moderate income persons for single family housing and higher education; loans to developers for multifamily housing; and private and public university buildings.

There are currently 15 different State debt issuers that have been authorized to sell various types of obligations. Table 3-1 presents a list of each issuer and the type of debt each has issued.

**Table 3-1
State Debt Issuing Agencies**

<u>Issuer</u>	<u>Tax-Supported Debt</u>	<u>Revenue Debt (State Credit Support)</u>	<u>Agency Revenue Debt</u>	<u>Conduit Debt</u>
Airport Corporation* (1)			X	
Clean Water Finance Agency				X
Convention Center Authority	X			
Economic Development Corporation	X	X	X	
Health and Education Building Corp.				X
Housing, Mortgage, and Finance Corp.	X	X	X	X
Industrial Facilities Corp.		X		X
Narragansett Bay Commission			X	
Resource Recovery Corporation			X	
State of Rhode Island-Capital Leases	X			
State of Rhode Island-GO Bonds	X			
State Universities and Colleges			X	
Student Loan Authority				X
Turnpike and Bridge Authority			X	
Water Resources Board			X	X

* The State has outstanding general obligation bonds issued on behalf of this agency.

(1) Borrows through the Economic Development Corporation.

Tax-Supported Debt: FY07 to FY11

Tax-Supported Debt includes general obligation bonds and bonds payable from leases which are subject to appropriation from the State's general fund. Credit ratings for this debt are largely dependent on the general fiscal condition of the State, amount of Tax-Supported Debt currently outstanding, the characteristics of the specific tax that is pledged for repayment, and the economic conditions of the State.

Table 3-2 presents the amounts and types of Tax-Supported Debt for the five years ending June 30, 2011 with resulting debt ratios. For FY11, the State's Debt to Personal Income ratio of 3.9% and Debt Service to Revenue ratio of 6.7% were in compliance with the Credit Guideline maximums of 6.0% and 7.5%, respectively. A detailed statement of Outstanding Tax-Supported Debt (actual) as of June 30, 2011 is presented in Appendix A.

Table 3-2
Tax-Supported Debt: Fiscal Years 2007 - 2011
 (dollars in millions, principal amount)

Fiscal Years	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>CAGR</u> <u>FY 07 - 11</u>
General Obligation Bonds	\$ 913.5	\$ 997.1	\$ 1,036.2	\$ 1,118.0	\$ 1,049.4	3.5%
Capital Leases	252.6	226.0	267.1	254.7	233.6	-1.9%
Convention Center Authority	280.0	271.0	263.8	268.3	259.6	-1.9%
Economic Development Corp.	147.0	142.6	286.5	259.9	238.4	12.8%
R.I.H.M.F.C. Neighborhood Opp. Hsing Prog.	15.5	18.2	13.2	8.4	3.5	-31.1%
Refunding Bond Authority (1)	42.7	24.2	6.0	-	-	-
Gross Tax-Supported Debt	\$ 1,651.3	\$ 1,679.1	\$ 1,872.8	\$ 1,909.3	\$ 1,784.5	2.0%
Agency Payments	(28.9)	(27.8)	(26.6)	(25.4)	(24.1)	-4.4%
Net Tax-Supported Debt	\$ 1,622.4	\$ 1,651.3	\$ 1,846.2	\$ 1,883.9	\$ 1,760.4	2.1%
 Annual Net Tax-Supported Debt Service (2)	 \$ 174.8	 \$ 185.8	 \$ 196.7	 \$ 218.2	 \$ 212.8	 5.0%
 Debt Ratios: (3)						
Annual Debt Service / Revenues (7.5%)	5.2%	5.2%	6.0%	7.0%	6.7%	6.7%
Net Debt / Personal Income (5% - 6%)	3.9%	3.8%	4.2%	4.3%	3.9%	0.1%
Net Debt / Capita	\$ 1,540.5	\$ 1,571.5	\$ 1,757.0	\$ 1,789.8	\$ 1,672.0	2.1%
 Assumptions:						
Revenues (2), (4)	\$ 3,361.0	\$ 3,580.9	\$ 3,270.8	\$ 3,112.4	\$ 3,159.3	-1.5%
Personal Income	\$ 41,893.5	\$ 43,455.0	\$ 43,635.3	\$ 43,854.8	\$ 45,291.8	2.0%
Population (5)	1,053,136	1,050,788	1,050,788	1,052,567	1,052,886	0.0%

CAGR = Compound Annual Growth Rate

Source: FY 13 Capital Budget

(1) As of February 1, 2010, all bonds of the Authority were paid in full.

(2) FY 08 - FY 12 Capital Budgets.

(3) Based on Net Tax-Supported Debt which includes agency payments.

(4) Revenues include actual general revenues plus dedicated gas tax transfers.

(5) Population estimates for 2011 are from the U.S. Census Bureau, September 22, 2011.

As the result of an increase in General Obligation debt and Economic Development Corporation debt, total Net Tax-Supported Debt increased by a CAGR of 2.1% from FY07 to FY11. These increases were partially offset by a 31.1% CAGR decrease in R.I.H.M.F.C. Neighborhood Opportunities Housing Program debt. State personal income grew at an annual compound rate of 2.0% while revenues declined by 1.5% over the same period.

The Governor, with approval by the General Assembly, also authorizes certain departments to finance the acquisition of equipment and the acquisition and improvement of buildings by using capital leases. Capital leases have been used to finance various projects such as the Attorney General's office, the ACI Intake Center, the office complex at Howard Center for the Department of Labor and Training and power generation facilities at the State Colleges and Universities. These capital leases are considered Tax-Supported Debt by bond credit analysts.

The Economic Development Corporation (the "EDC") issues debt that will be paid from State taxes and revenues which represents 13.5% of Net Tax-Supported Debt. This debt contains unusual credit features, which obligate the State to pay debt service under certain expected circumstances. Two such issues (Fidelity and Fleet leases) carry a moral obligation pledge, which requires the State to appropriate funds in the event that certain job hiring targets are met. In the event performance targets are not met, the State is not obligated to pay under the agreements. The purpose of this type of performance-based credit structure is to foster economic development, and to justify such appropriations by the generation of incremental income tax receipts. For this reason, issuance must be carefully monitored and measured for budget purposes.

Projected Tax-Supported Debt: FY12 to FY16

Using figures provided by the State Budget Office, an estimate of the Tax-Supported Debt for the FY12 - FY16 period has been developed along with a forecast of certain debt ratios.

Table 3-3						
Tax-Supported Debt: Fiscal Years 2012 - 2016						
(dollars in millions, principal amount)						
Fiscal Years	2012	2013	2014	2015	2016	CAGR FY 12 - 16
General Obligation Bonds	\$ 1,119.4	\$ 1,187.4	\$ 1,171.4	\$ 1,134.3	\$ 1,103.8	-0.4%
Capital Leases	267.5	254.0	229.7	205.8	176.8	-9.8%
Convention Center Authority	250.5	240.9	230.9	220.3	209.2	-4.4%
Economic Development Corp.	259.3	236.1	251.8	257.9	299.1	3.6%
R.I.H.M.F.C. Neighborhood Opp. Hsing Prog.	-	-	-	-	-	-
Gross Tax-Supported Debt	\$ 1,896.7	\$ 1,918.4	\$ 1,883.8	\$ 1,818.3	\$ 1,788.9	-1.5%
Agency Payments	(22.8)	(21.3)	(19.8)	(18.2)	(16.5)	-7.8%
Net Tax-Supported Debt	\$ 1,873.9	\$ 1,897.1	\$ 1,864.0	\$ 1,800.1	\$ 1,772.4	-1.4%
Annual Net Tax-Supported Debt Service (1)	\$ 217.7	\$ 235.5	\$ 237.6	\$ 256.4	\$ 261.0	4.6%
Debt Ratios: (2)						
Annual Debt Service / Revenues (7.5%)	6.5%	6.7%	6.6%	7.0%	7.1%	2.0%
Net Debt / Personal Income (5% - 6%)	4.0%	3.9%	3.7%	3.4%	3.2%	-5.6%
Net Debt / Capita	\$ 1,779.8	\$ 1,801.8	\$ 1,770.4	\$ 1,709.7	\$ 1,683.4	-1.4%
Assumptions:						
Revenues	\$ 3,338.7	\$ 3,503.0	\$ 3,599.7	\$ 3,652.6	\$ 3,696.3	2.6%
Personal Income	\$46,539.9	\$48,467.1	\$50,460.0	\$52,923.2	\$55,377.1	4.4%
Population (3)	1,052,886	1,052,886	1,052,886	1,052,886	1,052,886	0.0%
CAGR = Compound Annual Growth Rate						
Source: FY 13 Capital Budget						
(1) Projected Net Tax-Supported Debt Service. FY 13 Capital Budget, page B-14.						
(2) Based on Net Tax-Supported Debt which includes agency payments.						
(3) Population estimates are from the U.S. Census Bureau, September 22, 2011.						

Gross Tax-Supported Debt (excludes adjustments for agency payments) is projected to decrease from \$1,896.7 million in FY12 to \$1,788.9 million in FY16.

State Supported Revenue Debt

State Supported Revenue Debt is payable from specified revenues pledged for debt service which are not general taxes and revenues of the State. The State provides additional credit support to repay this debt only if the pledged revenues are insufficient to meet scheduled debt service payments.

The State provides credit support in a variety of forms. For purposes of this report, State Credit Support is broadly defined to include a contingent commitment to make annual appropriations under a lease, a contingent commitment to seek appropriations to replenish a special debt reserve, direct guarantees of debt payments, commitments to pay all or a portion of debt service under certain conditions, and commitments to provide other payments which indirectly secure or directly pay debt service.

A contingent commitment to seek appropriations to replenish a special debt reserve is known as a “moral obligation” and has special meaning to credit analysts. State laws that authorize moral obligation debt require notification by the Governor to the General Assembly when a deficiency in a special debt service reserve has occurred. The Governor then is required to request an appropriation to replenish the reserve to its required level. Credit analysts view “moral obligation” bonds as a contingent state obligation even though the legislative body is not contractually required to make the requested appropriation.

State Supported Revenue Debt represents a substantial contingent obligation of the State of \$282.7 million at June 30, 2011, down from \$314.0 million at June 30, 2010. While this type of debt is intended to be paid from dedicated revenues generated from financed projects, the State has provided credit support to additionally secure this debt. Because of the implied financial commitment of State support in the event of any unanticipated revenue shortfall, the level of this debt is an important consideration for the credit ratings of the State’s Tax-Supported Debt. Table 3-4 presents the amounts and types of State Supported Revenue Debt for the five years ending June 30, 2011.

Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11
EDC - Providence Place Mall	33.7	32.1	30.4	28.6	26.7	-5.7%
R.I. Housing	292.5	321.8	285.3	267.3	235.2	-5.3%
Industrial Recreational Building Authority - Insured						
Industrial Facilities Corporation	13.2	10.9	14.1	18.1	20.8	12.0%
Total	\$ 339.4	\$ 364.8	\$ 329.8	\$ 314.0	\$ 282.7	-4.5%
CAGR = Compound Annual Growth Rate						
Source: Treasury Survey of R.I. Quasi-Public Corporations.						

The largest component of State Supported Revenue Debt is the moral obligation debt of Rhode Island Housing, which has decreased by 57.3 million (CAGR of 5.3%) since 2007. State Supported Revenue Debt decreased by an annual compound rate of 4.5% for the period from FY07 to FY11.

The Rhode Island Industrial Facilities Corporation (“RIIFC”) issues bonds which are secured by loans and mortgages of private borrowers, but the bonds may be additionally secured by a voter authorized commitment provided by the Industrial-Recreational Building Authority (“IRBA”) which is funded by State appropriations. The portion of RIIFC’s debt guaranteed by IRBA is shown in this category.

The EDC is authorized to secure certain of its revenue bonds with the State moral obligation with the approval of the Governor and as of FY00, all debt issues previously secured under the traditional moral obligation pledge had been paid off. However, there were additional issues authorized by the General Assembly secured by the State’s Moral Obligation, including \$75 million Job Guaranty Program Revenue Bonds issued in FY11 and an additional 5.5 million were issued in FY12.

Agency Revenue Debt

Agency Revenue Debt is similar to the previous classification, except that the State has not provided any form of credit support and no general taxes or revenues are pledged for payment of these bonds. This type of debt is isolated from the State's general credit, but because the borrowers are agencies or corporations created by the General Assembly, this debt is not as removed as Conduit Debt.

Investors would expect that the State would take no actions which would cause these bond issuers financial harm, and the State has no legal responsibility to prevent financial defaults. However, as a practical matter, the State facilities which are financed in this manner, such as the University of Rhode Island, the Claiborne Pell and Mt. Hope Bridges, and the T.F. Green Airport expansion, are important public facilities, the use of which the State would not likely surrender in the event that the pledged revenues were insufficient to pay debt service. For this reason, this type of debt is important to the State's credit standing.

The State has issued general obligation bonds to finance facilities of several of the agencies shown in Table 3-5. Only the Revenue Debt of these agencies is presented in Table 3-5, and any other debt is presented in the sections relating to Tax-Supported Debt. Table 3-5 presents the amounts and types of Agency Revenue Debt for five fiscal years ending June 30, 2011.

Table 3-5						
Agency Revenue Debt: Fiscal Years 2007 - 2011						
(dollars in millions, principal amount)						
Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11
Airport Corporation	\$ 308.0	\$ 334.8	\$ 327.7	\$ 319.7	\$ 309.7	0.1%
Economic Development Corporation	67.8	77.2	94.4	94.0	97.5	9.5%
EDC - GARVEE Bonds, Federally Funded	207.8	285.5	427.4	400.5	372.3	15.7%
R.I. Housing	5.0	5.0	5.0	5.0	5.0	0.0%
Narragansett Bay Commission	444.7	463.2	444.0	410.1	422.4	-1.3%
Resource Recovery Corporation	16.2	14.5	14.8	14.0	13.1	-5.2%
State University and Colleges	199.3	195.1	222.6	283.1	276.2	8.5%
Turnpike and Bridge Authority	27.8	25.7	23.6	70.7	69.2	25.6%
Water Resources Board	8.3	7.5	5.8	4.9	4.1	-16.2%
Total	\$ 1,284.9	\$ 1,408.5	\$ 1,565.3	\$ 1,602.0	\$ 1,569.5	5.1%
CAGR = Compound Annual Growth Rate						
Source: Treasury Survey of R.I. Quasi-Public Corporations.						

The Turnpike and Bridge Authority experienced the largest increase of 25.6% followed by the EDC – GARVEE Bonds at 15.7%. Next was the Economic Development Corporation which increased by 9.5% and the State University and Colleges which increased by 8.5% because of various construction and improvement projects. Overall, Agency Revenue debt grew at a compound annual rate of 5.1% from FY07 - FY11. Because payment of this category of debt is supported by fees, charges, or other revenues, an increase in this type of debt may be considered as one indicator of economic growth. However, either a stable or growing economy is needed to support such debt.

Conduit Debt

Conduit Debt is issued by a state agency on behalf of borrowers, which include businesses, health care institutions, private higher education institutions, local governments, and qualified individuals (loans for housing and higher education purposes). These borrowers are able to borrow at the favorable tax exempt interest rates under the federal tax laws by having a State agency issue bonds on their behalf.

Conduit Bonds are payable from repayment of loans by the borrowers and are independent of the State's credit. Investors would not expect any assistance by the State in the event the borrower experienced financial difficulties or if the debt were to default. None of the debt presented in Table 3-6 is secured by any form of State Credit Support.

Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11
Clean Water Finance Agency	\$ 576.9	\$ 631.3	\$ 602.6	\$ 652.7	\$ 671.2	3.9%
Health and Educational Building Corporation	1,908.0	2,225.4	2,377.6	1,793.7	2,574.5	7.8%
R.I. Housing	1,234.5	1,289.6	1,293.7	1,445.1	1,416.5	3.5%
Industrial Facilities Corporation	105.2	86.1	89.3	95.3	80.8	-6.4%
Student Loan Authority	889.6	946.8	1,046.3	1,331.4	1,026.6	3.6%
Water Resources Board	3.0	2.0	1.0	-	-	-100.0%
Total	\$4,717.2	\$5,181.2	\$5,410.5	\$5,318.2	\$5,769.6	5.2%
CAGR = Compound Annual Growth Rate						
Source: Treasury Survey of R.I. Quasi-Public Corporations.						

Conduit Debt, which represents the largest category of debt, grew at a compound annual rate of 5.2% from FY07 - FY11. The agencies which experienced the most significant growth in debt were the Health and Educational Building Corporation and the Clean Water Finance Agency with compound annual growth rates of 7.8% and 3.9% respectively. The Student Loan Authority and R.I. Housing debt levels have also been on the rise, but at a slower rate.

Local Government Debt

Local governments issue various types of debt which may be secured by a general obligation of the local government or may be payable from a specific revenue source.

Table 3-7 presents the amounts of Local Government Debt for the five years ending June 30, 2011. This table does not include the debt of certain regional and municipal authorities including the Bristol County Water Authority, the Foster Gloucester Regional School District, Kent County Water Authority, and the Providence Public Building Authority.

Table 3-7							
Local Government Debt: Fiscal Years 2007 - 2011							
(in millions)							
Fiscal Years	2007	2008	2009	2010	2011	CAGR	
						FY 07 - 11	
Local Government Debt	\$ 1,498.5	\$ 1,713.7	\$ 1,692.0	\$ 1,767.6	\$ 1,821.3	5.0%	
CAGR = Compound Annual Growth Rate							
Source: Office of the General Treasurer and the Audited Financial Statements of the 39 Cities and Towns.							

Local government debt includes general obligation bonds and notes, revenue bonds, and capital leases of Rhode Island's 39 local governments. During the five years shown in Table 3-7 this debt grew at a compound annual growth rate of 5.0%.

SECTION 4

Debt Policies and Practices

Importance of Debt Management

The State of Rhode Island and its local governments use debt to finance capital improvements and to make loans at tax exempt interest rates to various government, nonprofit, and private borrowers for capital investments for economic development and other public purposes. The ability to fund capital investments through borrowing is important because the State and its local governments do not have sufficient cash reserves or dedicated revenue resources necessary to fund these expenditures. Of course, not all capital investments are funded or should be funded with debt. Current revenues and cash reserves also are and should remain as funding sources for capital improvements for the State and its local governments.

Maintaining an ability to borrow, often called “debt capacity,” is a critical resource for most state and local governments. Without debt capacity the State may not be able to pay for restoration of aging infrastructure and make new capital investment. Public capital investment attracts private capital to be invested, which creates employment and a high quality of life for the citizens of the State. Capital investment in transportation infrastructure, including highways, airports, and ports, is a basic building block for the State’s economy. Other essential capital investments must be continually made for purposes such as water, wastewater, recreation, local schools, and higher education. The State’s capital budget lays out future State capital needs. Because of the State’s current debt profile, prudent debt management is critical to satisfying these capital investment needs.

Debt Limits and Targets

Setting debt targets is a policy exercise involving balancing the cost of debt against the need for debt financed capital improvements. Many states set limits on debt that is paid from state general taxes and revenues. Maintaining a high credit rating or improving an average rating is a key objective in limiting debt in most states. The PFMB has set debt limits based on personal income levels and debt service as a percentage of General Revenues. However, municipal/public credit ratings are based on not only debt levels, but also financial, economic and management characteristics of the jurisdiction. There are no fixed formulas for the optimal combination of these factors. In reality, some factors, such as the economy or demographics, are beyond the issuer’s control. However, because debt issuance can be controlled, most borrowers focus on debt levels as a critical rating factor. The principal benefit of higher credit ratings is that investors are willing to accept lower interest rates on highly rated debt relative to lower rated debt; thereby reducing the State’s borrowing costs.

Debt Capacity

For purposes of this analysis, debt capacity is a term used to define how much debt can be issued by the State or an agency of the State, either on an absolute basis or without adverse consequences to its credit rating or the marketability of its debt. Debt capacity is customarily evaluated in view of the income, wealth, or asset base by which the debt is secured or from which it is paid. With the variety of debt types, payment sources and legal means used to secure debt, there is no single measure of debt capacity to which all debt issued by all state agencies would be subject.

Rhode Island made presentations to the State’s credit rating agencies on several occasions in 2010 and 2011. The agencies were provided with an update of the State’s budget, economic development initiatives and current debt profile. The ratings were based on the State’s economic performance, effective management of the State’s financial operations, and success in reducing the State’s debt burden, economic development efforts and recent

pension reform. Post recalibration, Rhode Island's general obligation bonds are currently rated "Aa2/AA/AA" by Moody's Investors Service, Standard & Poor's and Fitch, respectively. It is important to note that the State maintained its ratings level during the period 2001-2004, when many states were downgraded or placed on credit watch. However, in November 2007 when the State again met with all three rating agencies, their focus was on the State's budget situation. While all three rating agencies rate Rhode Island in the "Double A" category, recent rating reports include warning signs. One rating agency noted the State's use of one-time tobacco revenues to balance the 2007 and 2008 budgets which evidenced "continuing financial strain at a time when most states are moving toward structurally balanced budgets." It is clear that the rating agencies will continue to scrutinize the budget process carefully. There is no doubt that the projected budget deficit and actions taken to continue to address the projected deficit will be an important rating consideration. The State's financial and budgeting practices and track record in reducing the debt burden and taking appropriate action in response to budget pressures have been recognized as credit strengths in the past. Challenges to the State's ratings are presented by the projected budget deficits in the out year forecast, a relatively weaker economy and declining revenues combined with budgetary pressure for human services, infrastructure needs and the ability to maintain adequate reserves. The State's response to these challenges will be closely monitored by the rating agencies. No longer can the State rely on one-time revenues to balance its budget. Table 4-1 presents the credit ratings for all states with general obligation debt outstanding.

Debt projections for FY12 through FY16, as presented in Table 3-3, indicate that Debt to Personal Income will decrease from 4.0% to 3.2% during this period. These projections also show Debt Per Capita decreasing by 1.4% from \$1,779.8 to \$1,683.4 over the same period.

Because the rating agencies also evaluate economic and demographic factors in their rating analyses, the State's economic and demographic growth relative to other states will be a key factor in future comparisons. Finally, while the State's Debt to Personal Income of 4.7% in FY11 compares favorably to Moody's 2011 peer group average of 5.2%, this ratio is high relative to Moody's 2011 median (includes all states) of 2.8%. Likewise, the State's FY11 Debt per Capita of \$1,997 compares unfavorably to the current Moody's median at \$1,117, but favorably to the 2011 Peer Group Average of \$2,500. Debt levels tend to be relatively higher in Rhode Island's Peer Group states in light of their aging infrastructure and practice of financing projects at the state level rather than at the municipal or county level. These comparisons indicate that even after projected debt ratio improvements, Rhode Island's debt profile will continue to remain high relative to other states. These projections support Rhode Island's continued discipline in debt management.

**Table 4-1
Long Term Credit Ratings
General Obligation Bonds**

	Moody's	S & P	Fitch
Alabama	Aa1	AA	AA+
Alaska	Aaa	AAA	AA+
Arizona	Aa3	AA-	NR
Arkansas	Aa1	AA	NR
California	A1	A-	A-
Colorado	Aa1	AA	NR
Connecticut	Aa3	AA	AA
Delaware	Aaa	AAA	AAA
Florida	Aa1	AAA	AAA
Georgia	Aaa	AAA	AAA
Hawaii	Aa2	AA	AA
Idaho	Aa1	AA+	AA
Illinois	A2	A+	A
Indiana	Aaa	AAA	AA+
Iowa	Aaa	AAA	AAA
Kansas	Aa1	AA+	AA
Kentucky	Aa2	AA-	AA-
Louisiana	Aa2	AA	AA
Maine	Aa2	AA	AA+
Maryland	Aaa	AAA	AAA
Massachusetts	Aa1	AA+	AA+
Michigan	Aa2	AA-	AA-
Minnesota	Aa1	AA+	AA+
Mississippi	Aa2	AA	AA+
Missouri	Aaa	AAA	AAA
Montana	Aa1	AA	AA+
Nebraska	Aa2	AAA	NR
Nevada	Aa2	AA	AA+
New Hampshire	Aa1	AA	AA+
New Jersey	Aa3	AA-	AA-
New Mexico	Aaa	AA+	NR
New York	Aa2	AA	AA
North Carolina	Aaa	AAA	AAA
North Dakota	Aa1	AA+	NR
Ohio	Aa1	AA+	AA+
Oklahoma	Aa2	AA+	AA+
Oregon	Aa1	AA+	AA+
Pennsylvania	Aa1	AA	AA+
Rhode Island	Aa2	AA	AA
South Carolina	Aaa	AA+	AAA
South Dakota	Aa2	AA+	AA
Tennessee	Aaa	AA+	AAA
Texas	Aaa	AA+	AAA
Utah	Aaa	AAA	AAA
Vermont	Aaa	AA+	AAA
Virginia	Aaa	AAA	AAA
Washington	Aa1	AA+	AA+
West Virginia	Aa1	AA	AA+
Wisconsin	Aa2	AA	AA
Wyoming	NR	AAA	NR
Rhode Island rating compared to other states:			
Above Rhode Island	31	28	29
Same as Rhode Island	12	15	8
Below Rhode Island	5	6	5
NR	1	0	7
Source: First Southwest Company - State Ratings as of 5/29/12.			

Tax-Supported Debt

Tables 4-2, 4-3, and 4-4 present the history for the key debt ratios for Rhode Island and the median level for all states as determined periodically by Moody's Investors Service. The peer states of Delaware, Connecticut, Massachusetts, Maine, New Hampshire, and Vermont were selected due to geographical proximity (the New England states), population (Delaware, Vermont, New Hampshire, Maine), age of infrastructure (all), and concentration of services at the state level (Delaware).

	RI									
	National		Moody's	Peer						
Year	RI	Rank	Median	State Ave	DE	CT	MA	ME	NH	VT
2001	5.3%	7th	2.1%	4.8%	5.5%	8.0%	8.5%	2.0%	1.5%	3.3%
2002	5.2%	7th	2.3%	4.7%	5.3%	8.0%	8.5%	1.9%	1.5%	3.0%
2003	5.0%	7th	2.2%	4.7%	5.0%	8.2%	8.5%	1.8%	1.4%	3.0%
2004	4.4%	12th	2.4%	4.7%	5.6%	8.4%	8.5%	1.8%	1.5%	2.5%
2005	4.3%	16th	2.4%	4.7%	5.5%	8.5%	8.5%	2.2%	1.3%	2.3%
2006	4.1%	13th	2.5%	4.8%	5.3%	8.0%	9.8%	2.0%	1.4%	2.2%
2007	4.6%	13th	2.4%	4.7%	5.5%	7.8%	9.4%	1.9%	1.3%	2.1%
2008	4.7%	12th	2.6%	4.6%	5.2%	7.3%	9.8%	1.9%	1.3%	2.0%
2009	4.5%	11th	2.5%	4.6%	5.4%	8.2%	8.9%	2.2%	1.3%	1.8%
2010	5.2%	13th	2.5%	5.0%	6.2%	8.7%	9.2%	2.2%	1.6%	1.8%
2011	4.7%	14th	2.8%	5.2%	6.8%	9.1%	9.4%	2.3%	1.8%	2.0%
Source:	Moody's Investors Service									
	May 22, 2012 - State Debt Medians Report									

Note: Due to variations in calculation methods used by Moody's, Rhode Island's debt ratios in this table are different than the same ratios which are presented in Table 3-2.

The Tax-Supported Debt to personal income ratio measures the State's debt paid from general taxes and revenues in comparison to personal income, which is considered to be a good measure of the State's aggregate wealth. Rhode Island's Net Tax-Supported Debt to Personal Income ratio had decreased every year from 2001 - 2006 and its ranking dropped from the 7th highest in the country to the 13th highest. The 2005 ratio of 4.3% improved due to Tobacco Securitization and was below the peer group average of 4.7%, but it still remains well above Moody's median of 2.4%. However, in 2011 the ratio increased to 4.7% giving Rhode Island a ranking of 14th highest. This indicates that Rhode Island's Tax-Supported Debt is a greater burden on the State's economy than is typical of most states. Personal income represents the wealth of the State which is taxed to support Tax-Supported Debt or could be taxed to support State Credit Supported Revenue Debt.

**Table 4-3
Comparison to Peer States
Net Tax-Supported Debt per Capita**

<u>Year</u>	<u>RI</u>	<u>RI National Rank</u>	<u>Moody's Median</u>	<u>Peer State Ave</u>	<u>DE</u>	<u>CT</u>	<u>MA</u>	<u>ME</u>	<u>NH</u>	<u>VT</u>
2001	\$ 1,497	7th	\$ 541	\$ 1,565	\$ 1,616	\$ 3,037	\$ 2,957	\$ 487	\$ 463	\$ 828
2002	\$ 1,552	7th	\$ 573	\$ 1,660	\$ 1,650	\$ 3,240	\$ 3,267	\$ 485	\$ 503	\$ 813
2003	\$ 1,508	7th	\$ 606	\$ 1,692	\$ 1,599	\$ 3,440	\$ 3,298	\$ 471	\$ 485	\$ 861
2004	\$ 1,385	9th	\$ 701	\$ 1,734	\$ 1,800	\$ 3,558	\$ 3,333	\$ 492	\$ 496	\$ 724
2005	\$ 1,402	11th	\$ 754	\$ 1,904	\$ 1,845	\$ 3,624	\$ 4,128	\$ 606	\$ 514	\$ 707
2006	\$ 1,687	9th	\$ 787	\$ 1,944	\$ 1,998	\$ 3,713	\$ 4,153	\$ 603	\$ 492	\$ 706
2007	\$ 1,766	9th	\$ 889	\$ 2,009	\$ 2,002	\$ 3,698	\$ 4,529	\$ 618	\$ 499	\$ 707
2008	\$ 1,812	9th	\$ 865	\$ 2,150	\$ 2,128	\$ 4,490	\$ 4,323	\$ 743	\$ 525	\$ 692
2009	\$ 2,127	9th	\$ 936	\$ 2,348	\$ 2,489	\$ 4,859	\$ 4,606	\$ 760	\$ 665	\$ 709
2010	\$ 2,191	10th	\$ 1,066	\$ 2,508	\$ 2,676	\$ 5,236	\$ 4,711	\$ 865	\$ 812	\$ 747
2011	\$ 1,997	12th	\$ 1,117	\$ 2,500	\$ 2,674	\$ 5,096	\$ 4,814	\$ 845	\$ 776	\$ 792

Source: Moody's Investors Service
May 22, 2012 - State Debt Medians Report

Note: Due to variations in calculation methods used by Moody's, Rhode Island's debt ratios in this table are different than the same ratios which are presented in Table 3-2.

The ratio of Tax-Supported Debt to population fails to consider the economic wealth that supports the debt or the portion of the State's budget used to pay debt service. This ratio shows that three of the six peer states (Delaware, Connecticut and Massachusetts), have levels of debt per capita above the national median. This may be due to the combined factors of age of infrastructure, low population, and the dependency on the state to shoulder greater financing responsibilities. Since 2001, Rhode Island's Net Tax-Supported Debt per Capita has consistently been below that of the peer state average.

**Table 4-4
Tax-Supported Debt Service as a Percent of General Revenues**

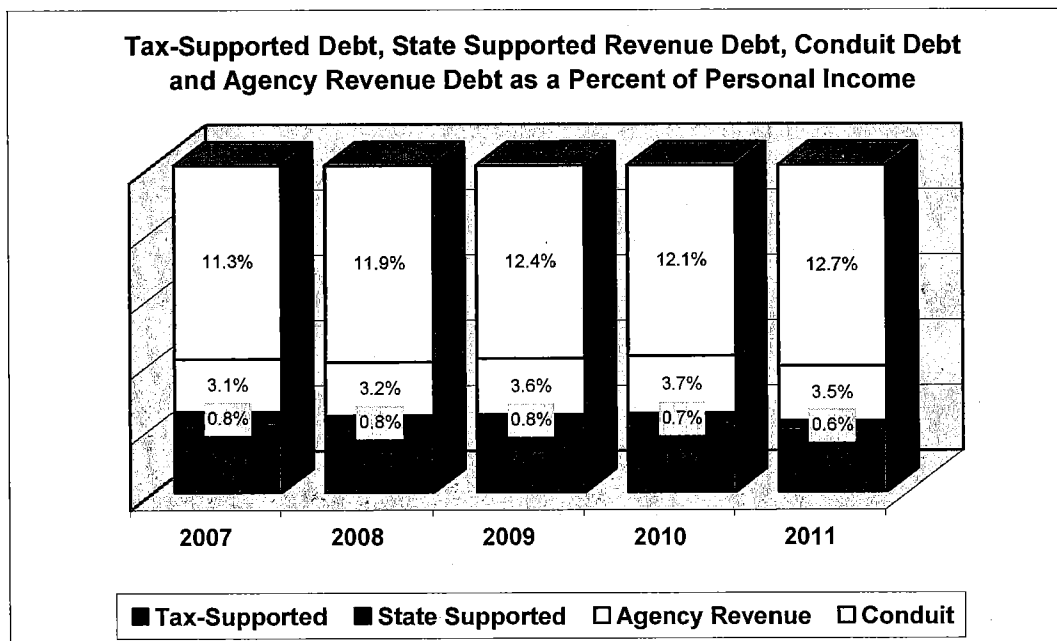
<u>Year</u>	<u>RI</u>
2007	5.2%
2008	5.2%
2009	6.0%
2010	7.0%
2011	6.7%

Source: FY 08 - FY 12 Capital Budgets.

Tax-Supported Debt Service to General Revenues is used for internal trend analysis, but no longer for peer group comparison analysis since the rating agencies no longer publish this data.

As Tables 4-2 and 4-3 show, Rhode Island has moderately high levels of Tax-Supported Debt according to these ratio measures. It should be noted, however, that tax supported debt as a per cent of personal income has declined somewhat since 2009 as shown in the chart below. High debt levels can lead to lower credit ratings, which result in higher borrowing costs, and a diminished financial capacity to respond to needed infrastructure improvements to support economic development.

As shown in the chart below, the total amount of Rhode Island’s Tax-Supported Debt, State Supported Revenue Debt, Agency Revenue Debt and Conduit Debt and its relationship to State personal income has increased from 19.0% of Personal Income in FY07 to 20.7% in FY11. This increase came as Personal Income grew at the compound annual growth rate of 2.0%.



Section 5

Recommended Priorities and Issues for 2012 and 2013

Based on the findings of this and the preceding Debt Management Reports, the following debt management priorities are recommended for 2012 and 2013.

1. Institutionalize and continue to improve Disclosure Practices

Improved Disclosure has been one of the General Treasurer's top priorities. During FY 2011, the State retained Special Disclosure Counsel and reconstituted its Disclosure Working Group. Regular training for Staff will be in place by the end of FY 2011. Training was expanded to include state agencies during FY 2012 and will be offered to municipalities in FY 2013. The Municipal Markets place increasing importance on Issuer Disclosure Information, not only when bonds are issued, but on a continuing basis. The State will consider the white papers being developed by the National Federation of Municipal Analyst and the National Association of Bond Lawyers in improving Disclosure Practices. In addition to offering training, the State will offer to extend Disclosure expertise to municipalities and other issuers in Rhode Island.

2. Enhanced Investor Relations Program

It is recommended that the State continue to improve its Investor Relations program to enhance the participation of Rhode Island "retail" investors in the purchase of State issued debt and to respond to the information needs of institutional investors. This effort will also serve to provide appropriate information to the marketplace on an ongoing basis. This initiative requires the assistance of the State's Bond Counsel, Disclosure Counsel, Special Disclosure Counsel and Financial Advisor. Market developments over the past few years have made analysis of the issuer's underlying credit more important to the investment decision. Therefore, improved Disclosure and Investor Relations can enhance an issuer's place in the market. As a first step, the Treasurer's office upgraded its website and added an investor relations portal. In addition, investor road shows, both in person and web-based have been undertaken, as well as direct outreach to major institutional investors.

3. Continued Emphasis on Rating Agency Communication and Debt Management

Rhode Island's improved debt position relative to the 50 states over the past decade is the product of policies and fiscal discipline adopted after the State's debt burden peaked in the early '90s. Rhode Island's relative position nationally improved from 7th highest ratio of debt to personal income in 2001 to 14th highest in 2011. The State's debt management policies included greater scrutiny of debt issues, the development of debt level benchmarks and refinement of the capital budgeting process. Rhode Island has lived up to its commitment to reduce its debt burden and is now realizing the benefits of this consistent discipline. Recent changes in rating agency criteria have incorporated Pension and OPEB liabilities in the analysis of overall debt burden. Rhode Island's past efforts related to retiree health care and its pension systems have been a positive development. However, more progress needs to be made in this area to manage future liabilities.

The credit guidelines and more conservative debt ratio targets approved by the PFMB in June 2000 provided the structure necessary to evaluate debt trends for the past 12 years. It is also appropriate, however, to review those guidelines in the context of new rating agency criteria and economic conditions and going forward, to look broadly at the debt approval process of the State and quasi-public agencies for opportunities to improve the review process and to strengthen controls.

Maintenance of the State's AA category ratings is more important now than ever before, as credit spreads are at their widest levels in decades and credit enhancement is only thinly available. Challenges to the State's ratings include a weak economy and declining revenues, budgetary pressure for human services, infrastructure needs, and the ability to maintain adequate reserves. The State's responses to these challenges will be closely monitored by the rating agencies. During periods such as these, regular communication with the rating analysts is critical and the State will continue to meet with the rating agencies on a regular basis and not solely in connection with the issuance of debt.

4. Sponsor Educational Programs for Municipalities

The PFMB can provide a much-needed service in offering continuing education on topical issues to municipal officers. Initiatives in this area have continued. In 2012, the Office of the General Treasurer hosted meetings and seminars for municipalities on pension reform and investments. In January 2011, the Office of the General Treasurer participated in a panel discussion for municipal officials at the Rhode Island League of Cities and Towns annual trade show on OPEB liabilities and funding. In February 2010, the Office participated in a RI League panel discussion for municipal officials on ARRA related financing opportunities. In October 2008, the Office of the General Treasurer hosted a seminar for Municipal and State officials. In the past, staff from the Office of General Treasurer worked with municipal finance officers and the Rhode Island Public Expenditure Council ("RIPEC") to develop a "Municipal Fiscal Healthcheck" to provide uniform data on the fiscal practices, policies, and status of all municipalities. The Office of the General Treasurer also supports the efforts of the Rhode Island Government Finance Officers Association ("RIGFOA") and has been involved in reviewing legislation to improve local borrowing practices, making presentations at RIGFOA meetings and the development of programs for RIGFOA members. In past years, topics included the State Retirement System, Cash Management and Other Post Employment Benefits. Future topics will include Performance Measures and Benchmarks, Disclosure Practices and Pension and OPEB Reform.

5. Explore Alternative Funding Mechanisms for Major Transportation and Infrastructure Projects

The State's Capital Budget and Transportation Improvement Plan ("TIP") have included significant increases in capital spending for major infrastructure projects such as the relocation of Route I-195. Revenues from the gasoline tax provide support for Transportation projects and the State General Fund. That revenue source has not kept pace with DOT's budget with debt service on General Obligation Bonds sold to prove the State match for Federal Highway funds requiring an increasing portion of the allocation. Dedication of additional revenues to Transportation will reduce the State's reliance on debt to provide State match and foster the stated PFMB and State goals of reducing or moderating Rhode Island's reliance on tax-supported debt for such projects. The PFMB should also monitor the work of Treasury staff and the State Administration to explore innovative funding mechanisms for major infrastructure projects. For example, Treasury staff reviewed the Garvee and Motor Fuel Tax bond issue structures as part of the November 2003, March 2006 and April 2009 issues. The State's efforts to wean the DOT from borrowing for State match for Federal Highway funds through the allocation of certain fees and RICAP funds to that purpose is a credit positive.

Several states explored public private partnerships or privatization of certain government assets to finance and/or manage certain projects such as roads and bridges. While private management can be a benefit with appropriate oversight, leveraging government assets often results in the loss of control over the project as well as user fees and costs to constituents. Recent trends in the credit markets increased the cost differential between

conventional financing and private financing. All such factors must be considered prior to moving forward with such an initiative.

6. Responding to Changes in the Municipal Bond Market and Regulatory Environment

The global credit crisis of 2008 had a major impact on the municipal bond market. The ability to access the capital markets has become increasingly challenging for issuers such as the State. The demise of the municipal bond insurance industry coupled with the credit squeeze and the notable absence of several major investment banking firms will have an impact on the State as it seeks to finance its capital needs. The State successfully sold its Tax Anticipation Notes for FY 2009 and 2010 and Certificates of Participation for new projects during the past year. Navigating these elements will continue to be a significant priority for the State to insure continued access to capital at affordable levels.

The Dodd-Frank Wall Street Reform and Consumer Protection Act includes many provisions that will have an impact on the municipal market including banking provisions and regulation and registration of municipal finance advisors. The Municipal Securities Rulemaking Board has new powers relating to issuers and advisors and the State will need to monitor these developments closely.

7. Monitor subsidies relating to American Recovery and Reinvestment Act of 2009 programs

The American Recovery and Reinvestment Act (ARRA) of 2009 included several municipal bond provisions that can benefit the State and its agencies and municipalities. The Office of the General Treasurer was involved in evaluating the applicability of Build America Bonds, Recovery Zone Bonds and Qualified School Construction Bonds. In 2010, the State acted quickly to take advantage of the provisions for Recovery Zone Bonds or “Super BABs” which provided a 45% subsidy off a taxable interest rate. It will be important to monitor the procedures for applying the federal subsidy for each interest payment.

8.

Monitor Moral Obligation Debt More Closely

The EDC Job Guaranty Revenue Bonds funded a loan to a private company. Less than two years after the loan was made, that company filed for bankruptcy. It is the recommendation of the PFMB that the EDC or any other issuer of Moral Obligation Bonds require quarterly financial reports from the borrowers and report annually to the General Assembly on the status of the borrower payments.

EXHIBIT A

Schedule of Tax Supported Debt

State of Rhode Island - Office of the General Treasurer
 Schedule of Tax Supported Debt
 As of 6/30/12

General Obligation Bonds		Description of Issue	Year Issued	Maturity Date	Principal Paid in FY 12	Interest Paid in FY 12	Principal Outstanding 6/30/2012	Interest Outstanding 6/30/2012
G.O. CCDL of 2001, Refunding Series A	2001		8/25/2011	15,510,000.00	1,081,775.00	0.00	0.00	0.00
G.O. Tax Anticipation Notes - Fiscal Year 2012	2012		6/29/2012	200,000,000.00	2,688,888.89	0.00	0.00	0.00
G.O. CCDL of 2002, Series B	2002		11/1/2012	3,360,000.00	259,000.00	2,070,000.00	51,750.00	0.00
G.O. CCDL of 2002, Refunding Series C	2002		11/1/2013	6,445,000.00	897,881.25	13,880,000.00	737,887.50	0.00
G.O. CCDL of 2008, Refunding Series A	2008		7/15/2014	4,745,000.00	910,125.00	15,830,000.00	1,215,000.00	0.00
G.O. CCDL of 2005, Refunding Series B	2005		8/1/2014	1,145,000.00	176,056.26	3,710,000.00	236,746.89	0.00
G.O. CCDL of 2004, Refunding Series B	2004		8/1/2015	7,535,000.00	2,298,987.50	42,225,000.00	2,912,625.00	0.00
G.O. CCDL of 2011, Refunding Series B	2011		8/1/2015	0.00	409,440.69	23,780,000.00	2,206,825.00	0.00
G.O. CCDL of 2004, Series A	2004		2/1/2016	3,650,000.00	2,614,825.00	7,350,000.00	717,575.00	0.00
G.O. CCDL of 2005, Series C	2005		2/15/2016	3,820,000.00	3,297,675.00	12,620,000.00	1,740,750.00	0.00
G.O. CDL of 2007, Series B (Federally Taxable)	2007		8/1/2017	765,000.00	321,467.50	5,695,000.00	976,076.25	0.00
G.O. CDL of 2008, Series C (Federally Taxable)	2008		2/1/2018	805,000.00	420,771.25	6,225,000.00	1,396,353.00	0.00
G.O. CCDL of 2008, Refunding Series D	2008		2/1/2018	1,405,000.00	477,525.00	9,690,000.00	1,613,500.00	0.00
G.O. CCDL of 2005, Refunding Series D	2005		7/15/2018	2,975,000.00	2,026,962.50	41,060,000.00	6,322,175.00	0.00
G.O. CCDL of 2005, Refunding Series A	2005		8/1/2018	60,000.00	2,542,123.76	51,290,000.00	11,872,394.44	0.00
G.O. CDL of 2010, Series D (Federally Taxable)	2010		4/1/2020	2,250,000.00	741,290.10	19,205,000.00	3,506,985.84	0.00
G.O. CCDL of 2010, Refunding Series A	2010		10/1/2020	1,650,000.00	3,402,100.00	77,310,000.00	14,397,562.50	0.00
G.O. CCDL of 2006, Refunding Series A	2006		8/1/2022	155,000.00	3,250,612.50	68,440,000.00	20,168,518.77	0.00
G.O. CCDL of 2005, Series E	2005		11/1/2025	3,570,000.00	3,529,271.26	45,915,000.00	16,760,515.75	0.00
G.O. CCDL of 2006, Series C	2006		11/15/2025	3,905,000.00	3,875,566.25	80,360,000.00	29,607,605.00	0.00
G.O. CDL of 2006, Series B	2006		8/1/2026	800,000.00	757,428.76	16,980,000.00	6,379,430.70	0.00
G.O. CDL of 2007, Series A	2007		8/1/2027	4,210,000.00	5,227,177.50	104,220,000.00	46,451,673.75	0.00
G.O. CCDL of 2012, Refunding Series A	2012		8/1/2027	0.00	0.00	122,950,000.00	47,314,259.87	0.00
G.O. CCDL of 2008, Series B	2008		2/1/2028	3,125,000.00	4,085,025.00	76,815,000.00	39,271,000.00	0.00
G.O. CCDL of 2010, Series B (Tax Exempt)	2010		4/1/2030	1,345,000.00	1,800,700.00	37,930,000.00	19,263,900.00	0.00
G.O. CDL of 2010, Series C	2010		4/1/2030	0.00	4,479,957.00	80,000,000.00	62,776,733.62	0.00
G.O. CCDL of 2011, Series A	2011		8/1/2031	0.00	3,048,024.13	145,035,000.00	90,092,968.75	0.00

Total General Obligation Bonds

273,230,000.00 54,620,657.10 1,110,585,000.00 427,990,812.63

Description of Issue	Year Issued	Maturity Date	Principal Paid in FY 12	Interest Paid in FY 12	Principal Outstanding 6/30/2012	Interest Outstanding 6/30/2012
Capital Leases						
LPC, State Vehicles Project - 2005 Series C	2005	4/1/2012	795,000.00	27,825.00	0.00	0.00
C.O.P. in L.P.A. (State Vehicles Projects), 2002 Series A	2002	12/15/2012	270,000.00	22,477.50	270,000.00	5,670.00
LPC, State Vehicles Project - 2006 Series A	2006	4/15/2013	465,000.00	57,222.00	490,000.00	19,404.00
LPC, State Vehicles Project - 2007 Series C	2007	5/1/2014	405,000.00	81,000.00	810,000.00	48,600.00
LPC, Attorney General's Building - 2007 Refunding Series G	2007	10/1/2015	305,000.00	85,902.50	1,145,000.00	74,582.50
LPC, Information Technology Project - 2009 Series A	2009	4/1/2016	1,700,000.00	566,050.00	7,320,000.00	695,100.00
LPC, Howard Center Improvements - 2007 Refunding Series E	2007	10/1/2016	1,580,000.00	827,750.00	8,115,000.00	898,312.50
LPC, Shepard's Building - 2007 Refunding Series F	2007	10/1/2016	2,160,000.00	1,360,000.00	13,060,000.00	1,713,250.00
LPC, Information Technology Project - 2007 Series A	2007	5/1/2017	2,895,000.00	1,188,925.00	9,475,000.00	1,367,062.50
LPC, Central Power Plant - 2007 Refunding Series D	2007	10/1/2020	1,485,000.00	1,495,087.50	16,735,000.00	3,542,406.25
LPC, Energy Conservation Project - 2009 Series B	2009	4/1/2021	750,000.00	890,075.00	10,115,000.00	2,563,387.50
LPC, Energy Conservation Project - 2007 Series B	2007	5/1/2023	750,000.00	903,762.52	10,005,000.00	2,611,756.34
LPC, Energy Conservation Project - 2007 Series B	2004	10/1/2023	2,605,000.00	3,982,541.25	42,110,000.00	13,314,390.00
LPC, Kent County Courthouse Project - 2004 Series A	2005	10/1/2024	2,160,000.00	4,060,400.00	40,290,000.00	14,487,600.00
LPC, Training School Project - 2005 Series A	2005	10/1/2024	930,000.00	1,473,341.27	16,380,000.00	5,413,649.46
LPC, Traffic Tribunal Project - 2005 Series B	2011	4/1/2026	1,910,000.00	1,396,507.50	30,070,000.00	6,236,800.00
LPC, Energy Conservation Project - 2011 Series A	2009	4/1/2029	1,060,000.00	2,810,300.00	27,410,000.00	14,774,587.52
			22,225,000.00	21,229,167.04	233,800,000.00	67,766,558.57
Total Capital Leases						
R.I. Economic Development Corporation						
Transportation Motor Fuel (C-10)	2003	6/15/2026	3,710,000.00	3,439,171.00	70,350,000.00	29,107,767.00
URI Power Plant (C-14)	1999	11/1/2019	835,000.00	456,285.00	8,360,000.00	1,984,785.00
Fidelity Building I (C-28)	1996	5/1/2021	1,123,745.00	1,364,781.00	15,585,984.00	6,846,037.00
Fidelity Building II (C-29)	2002	5/1/2027	311,292.00	642,762.00	8,643,065.00	5,667,737.00
Fleet Bank (C-30)	1997	5/1/2027	295,000.00	653,129.00	8,360,000.00	5,801,264.00
			6,275,037.00	6,556,128.00	111,299,049.00	49,407,590.00
Total R.I. Economic Development Corporation						
			9,110,000.00	14,030,282.00	250,510,000.00	150,555,826.00
Convention Center Authority (C-4)						
			310,840,037.00	96,436,234.14	1,706,194,049.00	695,720,787.20
Grand Total						

EXHIBIT B

Summary of Debt Issuances

The Public Finance Management Board
 Summary of Debt Issuance by Cities & Towns

100%	Date	Amount	City or Town	Type	Bond Counsel Fee	Description of Issue	Report of Final Sale Received
	1/13/11	1,380,000.00	Town of Smithfield, R. I.	G.O.	10,000.00	G.O. Taxable Bonds, 2011 Series B	1/20/11
	1/13/11	6,270,000.00	Town of Smithfield, R. I.	G.O.	10,000.00	G.O. Bonds, 2011 Series A	1/20/11
	1/19/11	6,800,000.00	Town of Cumberland	TAN's	6,500.00	G.O. Tax Anticipation Note, Series 2	5/26/11
	1/20/11	4,000,000.00	Town of North Providence	TAN's	15,000.00	G.O. Tax Anticipation Notes	1/27/11
	2/4/11	5,000,000.00	Town of Middletown	G.O.	17,464.00	G.O. Bonds dated 2/1/11	3/11/11
	2/8/11	33,500,000.00	Town of East Greenwich, R. I.	BAN's	15,500.00	G.O. Bond Anticipation Notes dated 2/9/11	3/3/11
	2/9/11	5,720,000.00	Town of Bristol, Rhode Island	G.O.	21,000.00	G.O. Bonds dated 2/17/11	2/18/11
	2/25/11	11,500,000.00	City of Woonsocket	G.O.	50,000.00	G.O. Deficit Bonds	5/5/11
	3/15/11	2,000,000.00	Town of Warren	G.O.	7,000.00	G.O. Clean Water Bonds dated 3/29/11	4/15/11
	3/20/11	3,070,000.00	Town of Bristol, Rhode Island	G.O.	15,000.00	G.O. Bonds dated 3/29/11	3/30/11
	3/22/11	3,095,505.00	City of Newport, Rhode Island	Revenue	15,000.00	Wastewater System Revenue Bonds (Taxable), 2011 Series A	4/15/11
	3/22/11	3,270,400.00	Town of Barrington, R. I.	G.O.	9,173.75	G.O. Clean Water Bonds dated 3/29/11	4/15/11
	3/24/11	2,902,500.00	Town of Lincoln, Rhode Island	Revenue	17,000.00	Wastewater System Revenue Bonds, 2011 Series A	4/15/11
	3/24/11	10,345,000.00	City of Newport, Rhode Island	Revenue	20,000.00	Wastewater System Revenue Bonds, 2011 Series B (Conduit Issue)	4/15/11
	3/24/11	23,000,000.00	City of East Providence, R. I.	Revenue	10,000.00	Wastewater System Revenue Bonds, 2011 Series A dated 3/29/11	4/15/11
	3/30/11	2,000,000.00	Town of Scituate, R. I.	TAN's	4,000.00	G.O. Tax Anticipation Notes	3/30/11
	4/1/11	11,600,000.00	City of Pawtucket, R. I.	TAN's	6,250.00	G.O. Tax Anticipation Notes dated 4/6/11	4/25/11
	4/8/11	736,250.00	Town of Warren	BAN's	5,500.00	G.O. Bond Anticipation Notes dated 4/26/11	4/28/11
	4/21/11	35,000,000.00	Providence Public Bldgs Auth	Revenue	94,235.72	G.O. Bond Anticipation Notes dated 4/26/11	10/25/11
	4/27/11	175,000.00	Cumberland Fire District	TAN's	2,100.00	G.O. Tax Anticipation Note	5/6/11
	4/28/11	4,330,000.00	Providence Fire District	BAN's	10,000.00	G.O. Bond Anticipation Notes dated 4/12/11	5/4/11
	5/18/11	16,990,000.00	City of Warwick, Rhode Island	G.O.	20,000.00	G.O. Refunding Bonds dated 5/26/11	6/8/11
	6/20/11	450,000.00	Town of New Shoreham	G.O.	3,000.00	G.O. Bonds	7/20/11
	6/28/11	9,000,000.00	City of Newport, Rhode Island	BAN's	15,500.00	G.O. Bond Anticipation Notes dated 7/7/11	7/26/11
	6/30/11	3,145,000.00	Providence Redevelopment Agency	Revenue	48,250.00	Umcore Project - Taxable Lease Revenue Bonds, 2011 Series 2	10/24/11
	7/15/11	250,000.00	Town of New Shoreham	G.O.	3,500.00	G.O. Bond Anticipation Note	9/26/11
	7/19/11	1,000,000.00	Town of Hopkinton, R. I.	G.O.	6,000.00	G.O. Bonds	8/29/11
	8/2/11	5,500,000.00	Town of Coventry, R.I.	TAN's	2,000.00	Taxable Tax Anticipation Notes	8/2/11
	8/16/11	300,000.00	Town of North Kingstown	Loan	600.00	Septic Revolving Fund Loan Agreement with R.I.C.W.F.A.	9/16/11
	8/16/11	6,000,000.00	City of East Providence, R. I.	BAN's	7,000.00	G.O. Bond Anticipation Notes dated 8/18/11	10/18/11
	8/19/11	614,000.00	Town of Exeter	G.O.	4,500.00	G.O. Refunding Bonds	10/12/11
	8/24/11	5,650,000.00	City of Pawtucket, R. I.	BAN's	10,250.00	G.O. Bond Anticipation Notes dated 8/25/11	8/31/11
	8/29/11	4,000,000.00	City of Woonsocket	BAN's	23,980.00	Wastewater System Revenue Bond Anticipation Note	9/27/11
	9/6/11	729,600.00	Town of Barrington, R. I.	G.O.	4,650.00	G.O. Bonds	12/20/11
	9/15/11	600,000.00	Pascoag Fire District	G.O.	4,000.00	G.O. Bonds	10/18/11
	9/15/11	1,000,000.00	Town of East Greenwich, R. I.	G.O.	10,300.00	G.O. Bonds	10/18/11
	9/19/11	5,105,000.00	City of Newport, Rhode Island	BAN's	11,000.00	Water System Revenue Bond Anticipation Notes, 2011 Series 1	10/28/11
	10/7/11	1,000,000.00	Bristol County Water Authority	Revenue	30,000.00	General Revenue Bonds, 2011 Series A dated 10/7/11	10/11/11
	10/18/11	7,485,000.00	City of Pawtucket, R. I.	Revenue	17,063.65	Water System Revenue Bonds	1/19/12
	10/18/11	13,770,000.00	Town of Coventry, R.I.	G.O.	25,000.00	G.O. Refunding Bonds dated 9/29/11	1/17/11
	10/24/11	2,000,000.00	City of East Providence, R. I.	Revenue	12,300.00	Water Revenue Bonds, 2011 Series A dated 11/4/11	1/19/12
	10/25/11	6,640,000.00	City of Newport, Rhode Island	Revenue	20,000.00	Water System Revenue Bonds, 2011 Series A dated 9/30/11	10/28/11
	11/14/11	5,890,000.00	Town of Cumberland	G.O.	25,000.00	G.O. Bonds, 2011 Series A and Refunding Series B	2/3/12
	11/14/11	10,500,000.00	Town of Cumberland	TAN's	5,000.00	G.O. Tax Anticipation Notes, Fiscal Year 2012, Series 1	5/2/12
	12/12/11	10,000,000.00	City of East Providence, R. I.	BAN's	11,275.00	G.O. Bond Anticipation Notes dated 12/15/11	3/28/12
	12/16/11	4,000,000.00	Town of North Providence	TAN's	12,249.49	G.O. Tax Anticipation Notes dated 12/21/11	5/3/12
	5/3/12	6,500,000.00	Town of Westerly, R. I.	BAN's	5,665.00	G.O. Bond Anticipation Notes dated 12/11/11	5/3/12

693,141.61

297,313,255.00

EXHIBIT C

Credit Rating Reports

Rhode Island & Providence Plantations; Appropriations; General Obligation; Moral Obligation

Primary Credit Analyst:

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Rhode Island & Providence Plantations; Appropriations; General Obligation; Moral Obligation

Credit Profile

US\$125.315 mil cons cap dev loan rfdg ser 2012A due 03/01/2023

<i>Long Term Rating</i>	AA/Stable	New
Rhode Island & Providence Plantations GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services has assigned its 'AA' long-term rating to Rhode Island & Providence Plantations' series 2012A general obligation (GO) refunding bonds. Standard & Poor's also affirmed its 'AA' rating on the state's GO bonds, its 'AA-' rating on the state's appropriation debt, and its 'A' rating on Rhode Island's moral obligation-backed bonds. The outlook on all ratings is stable.

The ratings reflect our opinion of Rhode Island's:

- Good income levels, with median household effective buying income at 103% of the national level;
- Good geographic location near the economies of eastern Massachusetts and eastern Connecticut; and
- Strong financial management and achievement of fully-funded general fund reserves in the two most recent fiscal years.

Partially offsetting the above strengths is our view of Rhode Island's:

- Projected budget gaps for fiscals 2014 through 2017 that reach about 15.6% of revenues in the last year and that could grow if economic conditions weaken more than projected;
- Recent multiyear trend of revenues falling below projections, resulting in general fund deficits in fiscals 2007 through 2009 and year-end fund balances below statutory requirements; and
- Significantly underfunded pension system, with funded ratios that declined significantly due to recently adopted changes.

The GO bonds are secured by the state's full faith and credit, the appropriation debt is subject to annual appropriation, and the moral obligation debt is secured by the state's moral obligation to refill the bonds' debt service reserve fund if it falls below the required maximum annual debt service. We understand that officials will use the series 2012A bond proceeds to refund about \$110 million of GO bonds outstanding and to restructure about \$23 million of transportation GO bonds outstanding. The refunding is projected to result in net present value savings of about \$9.0 million or about 8.2% of par. The restructuring reduces debt service in fiscals 2013 through 2015, with the debt service extended to 2028. State officials project the restructuring to result in a net present value loss of \$860,000 or 4.1% of par, with losses of about \$2.4 million per year in fiscals 2016 through 2023. Overall, officials project the combined refunding and restructuring to result in a net present value savings of \$8.2 million or 6.2% of par. The restructuring is intended to reduce the amount of GO debt that the state expects to be

self-supported by the department of transportation, due to transportation revenue declines.

Rhode Island ended fiscal 2011 with a fully funded stabilization fund of \$130.3 million (about 4% of general fund expenditures) and an additional unreserved general fund balance of \$64.2 million. The largest general revenue sources are the personal income tax (PIT) and the sales and use tax; in fiscal 2011, the former accounted for 33% of general revenues and the latter for about 26%. Fiscal 2011 included full actuarial funding of other postemployment benefits (OPEB) costs, which represented a \$7.9 million increase from the projected pay-as-you-go cost for the general revenue budget.

After multiple years of lowered revenue estimates, the May and November 2011 revenue estimating conferences resulted in modestly increased projections. The November conference revised the fiscal 2012 general fund projections upward by \$19.4 million from the May 2011 projections. The revised estimate of \$3.18 billion is \$111.7 million or 3.6% higher than the fiscal 2011 audited actual revenues. Through March, the fiscal 2012 general revenues were \$62.5 million or 3.0% above budget projections. The largest revenue sources were also both above budget projections: the personal income tax was 3.9% above budget and sales and use taxes were 0.3% above projections.

Officials projected the fiscal 2012 budget gap to be about \$300 million, or 9.3% of expenditures, at the time Gov. Lincoln Chafee's recommended budget was introduced, primarily due to a projected \$215 million loss of federal stimulus funding. The enacted budget passed by the state's General Assembly and signed by the governor made significant changes to the recommended budget, and the enacted budget did not include the governor's proposal to broaden the sales tax base to include more services and reduce the rate to 6% from 7%, which officials projected would increase fiscal 2012 revenues by \$164.8 million. The enacted budget closed the projected gap primarily with both recurring and nonrecurring revenue increases and expenditure reductions. The largest revenue and expenditure gap-closing measures in the enacted budget were:

- \$60.5 million of reductions in human service programs;
- \$57.2 million of estimated fiscal 2011 free surplus that was carried over to fiscal 2012;
- \$51.4 million of additional recurring revenue, per the May 2011 revenue estimate;
- \$32.0 million of one-time federal grant funding; and
- \$17.1 million from the inclusion of four previously exempt items in the sales and use tax base.

The enacted budget includes a \$5.5 million increase in payments-in-lieu-of-taxes to local governments, but did not include the governor's recommended \$4.9 million appropriation for the City of Central Falls. The enacted budget did include a \$10 million appropriation for distressed municipalities, equal to the fiscal 2011 level, although the General Assembly did not include the governor's recommended \$5.2 million increase to distressed municipality aid for the amended fiscal 2011 budget. The fiscal 2012 budget also fully funds the education funding formula that was enacted in June 2010. The state issued \$200 million of tax anticipation notes (TAN) in fiscal 2012, a reduction from the \$350 million issued in each of the previous three fiscal years, and officials project that the TAN issuance will again be smaller in fiscal 2013.

The fiscal 2013 governor's recommended budget closes a gap that was most recently estimated to be \$165.7 million, or about 5% of revenues, after agency current service requests. This gap projection was after the impact of pension reform legislation passed in late 2011, which is estimated to reduce expenditures by \$116.8 million. The 2013 budget proposes eliminating the gap with a combination of expenditure cuts and revenue enhancements, along with

the use of the projected fiscal 2012 ending balance of \$6.0 million. The recommended budget proposes \$92.9 million of revenue increases for fiscal 2013, the largest being a 2 percentage point increase in the meals and beverage tax -- which the budget estimated to generate \$39.5 million in additional revenue -- and the removal of the sales tax exemption for higher priced clothing and other sales and use tax changes, which are projected to increase revenues by \$27.1 million. The budget also projects that a tax amnesty program will generate \$10.9 million of additional revenues. In total, the 2013 budget proposal projects a 5.1% increase in general revenues from the fiscal 2012 level, driven primarily by a 5.1% increase in the personal income tax and an 11.3% increase in sales and use taxes after the proposed increases, or 3.1% projected sales and use tax growth before the effect of the proposed changes.

The budget proposes \$5.1 million of new expenditures and \$86.9 million of expenditure reductions from previously projected 2013 levels. In total, the budget projects fiscal 2013 general revenue expenditures to increase by \$96.4 million, or 3.0%, from the recommended supplemental 2012 levels. The largest expenditure increase is \$63.4 million in additional general revenue expenditures for state aid to cities and towns, although \$32.5 million of that increase is due to state general revenues replacing federal Education Jobs funding from fiscal 2012, and not an increase in total funds expenditures. The local aid funding fully finances the second year of the statewide school funding formula and includes an additional \$11.0 million increase to be distributed to underfunded districts. There is a \$6.4 million increase in higher education funding due to an increase in debt service at the public colleges and universities. The budget projects a fully funded budget stabilization reserve at the end of fiscal 2013, along with an additional ending surplus of \$1.4 million.

Rhode Island's long-range financial plan projects continued budget gaps. The plan includes a projection of legalized gambling in Massachusetts, which would reduce Rhode Island's gambling revenue, assuming no changes in the state's gaming options. The projected gaps are \$104 million for fiscal 2014 (3.5% of 2012 revenues), increasing to \$464.4 million for fiscal 2017 (15.6%), the final year of the plan. The revenue reduction from Massachusetts gaming is projected to begin at \$52 million in fiscal 2015 and rise to \$140 million in fiscal 2017.

The Rhode Island General Assembly passed the Rhode Island Retirement Security Act of 2011 (RIRSA) on Nov. 17, 2011, and the governor signed it on Nov. 18, 2011. The act makes significant changes to all of the plans the Employees' Retirement System of Rhode Island (ERSRI) administers, which include: ERSRI State Employees (including correctional officers and nurses); ERSRI Teachers; Municipal Employees Retirement System (MERS), including general employees and public safety; Judicial Retirement Benefits Trust; and State Police Retirement Benefits Trust. ERSRI's actuaries performed an actuarial analysis that indicates the act reduced the system's June 30, 2010, unfunded actuarial accrued liability (UAAL) by \$3.02 billion, from \$7.30 billion to \$4.29 billion. Rhode Island has full or partial funding responsibilities for the state employees, teachers, judges, and state police systems, and the analysis calculates the UAAL for those four systems to have decreased by \$2.76 billion, from \$6.87 billion to \$4.11 billion and the funding ratio improved to 59% from 49%. Officials indicate that the pension funding savings for the state government in fiscal 2013, including the state's share of teacher contributions, will be about \$240 million.

Based on the analytic factors we evaluate for states, on a scale on which '1' is the strongest, we have assigned Rhode Island a composite score of '1.9'.

Outlook

The stable outlook reflects our view that Rhode Island's government framework and financial management procedures are strong, as demonstrated by budget adjustments in recent years that have closed large gaps. We believe that the state's stabilization funding mechanism and ability to enact revenue and expenditure amendments with few limits should allow the state to maintain an adequate budgetary balance and liquidity position. We believe that recent large expenditure reductions, low pension funding levels, and a relatively weak economy make additional spending cuts or tax increases more difficult. We also believe that credit quality could come under pressure if revenue recovery is weaker than forecast and thus prevents the state from adjusting its budget, or from the implementation of the Budget Control Act of 2011. Should the federal reductions undermine the state's revenue performance, and if the state is unable to make sufficient adjustments to its budget, however, it could pressure the rating. We will continue to monitor these effects as they materialize, with a particular focus on the state's ability to absorb these reductions while maintaining structural balance, and the state's response will be integral to our maintenance of the rating.

Government Framework

In our view, the state has significant flexibility to increase the rate and base of its major revenues and also to decrease its expenditures. Rhode Island can raise its income and sales tax rates and base with a simple majority vote of the legislature and without voter approval. In our view, the state also has flexibility to decrease its major expenditures to local governments, and in recent years it made significant midyear decreases in its funding provided to local governments, demonstrating a willingness to reduce this funding in order to maintain its own financial position. Officials also have the ability to delay disbursements to later in a fiscal year, which provides some cash flow flexibility.

The state has a requirement that the governor and legislature prepare and enact balanced budgets. There is no voter initiative process in the state. Debt service can be paid without an appropriation budget, but does not have a first claim on revenues.

On a scale of '1' (strongest) to '4' (weakest), we have assigned a '1.2' to Rhode Island's government framework.

Financial Management

Standard & Poor's considers Rhode Island's financial management practices "strong" under its Financial Management Assessment methodology, indicating practices are strong, well embedded, and likely sustainable.

We consider the state's budget management to be good, featuring a consensus revenue and caseload forecasting procedure that meets at least twice a year, and can be convened at the request of any member. The forecasting committee consists of the chief fiscal staff of the offices of the executive branch and the two houses of the legislature. However, Rhode Island's structural budget performance has been below average in recent years in our opinion. The state's service levels are considered to be somewhat flexible, and the state has made cuts in its local aid in recent years in order to balance the budget.

On a scale of '1' (strongest) to '4' (weakest), we have assigned a '1.5' to Rhode Island's financial management.

Economy

Rhode Island's unemployment rate was 11.3% for 2011, one of the highest rates in the nation, after peaking at 11.6%. In the past five years, the state's population has increased by 0.4% from 2000 to 2010. State income levels have historically been on par with the nation's; in 2008, the state's household and per capita effective buying income levels were 103% and 104% of the national level, respectively.

IHS Global Insight Inc. indicates that the state's private sector employment contracted for six consecutive months through January 2012, with an average loss of 1.4% per month for November 2011 through January 2012, or 1,400 jobs over that period. Much of this loss was attributed to the leisure and hospitality sector. Despite the overall decline though, business services and manufacturing sectors have been adding jobs. IHS Global Insight projects that private-sector jobs will increase by 1.5% between fourth-quarter 2011 and fourth-quarter 2012, and the unemployment rate will end 2012 at 10.5%, which is elevated but a relative improvement. In addition, IHS Global Insight projects the main drivers of employment gains to be in the healthcare and administrative support sectors. Longer term, it projects payrolls to grow by 0.9% per year between 2011 and 2017, which it projects to be the slowest growth in the nation. In addition, the state is not projected to be at pre-recession employment levels until 2020.

On a scale of '1' (strongest) to '4' (weakest), we have assigned a '2.2' to Rhode Island's economy.

Debt And Liability Profile

Tax-supported debt

As of June 30, 2011, the state's total net tax-supported debt burden was 3.7% of personal income and about \$1,600 per capita. The fiscal 2011 carrying charge for tax-supported debt was about 6% of general governmental expenditures. Rhode Island improved its debt ratios in previous years by defeasing debt with the proceeds of a \$685 million tobacco securitization. As of fiscal 2011, about \$800 million of tobacco bonds were outstanding. The state has issued TANs annually since fiscal 2007, and the current \$200 million note matures on June 30, 2012. The amount of the fiscal 2012 TAN is lower than the fiscals 2009, 2010, and 2011 issues. Rhode Island has no exposure to interest-rate swaps, and its variable-rate debt was fully retired in December 2010. Debt service can be paid in the absence of an appropriation budget, but there is no other priority for the payment of debt before other general state expenditures. The state's debt amortization is at a level we consider above average, and officials estimate that new debt issuance is not likely to significantly outpace amortization in future years.

Pensions And Other Post Employment Benefits

The Rhode Island General Assembly passed RIRSA on Nov. 17, 2011, and the governor signed it on Nov. 18, 2011. The act makes significant changes to all of the plans the ERSRI administers, which include: ERSRI State Employees (including correctional officers and nurses); ERSRI Teachers; MERS, including general employees and public safety; Judicial Retirement Benefits Trust; and State Police Retirement Benefits Trust.

The primary changes from RIRSA are:

- The general state and municipal employees and teachers will change from a defined benefit plan to a hybrid plan

that combines a smaller defined benefit and a supplemental defined contribution element;

- The public safety plans, except for state police, will extend the retirement age and lower the benefit multiplier;
- Cost-of-living-adjustments (COLAs) will be suspended or reduced for years in which the funded ratio for the aggregated state employees, teachers, judges, and state police plans is lower than 80% funded;
- When COLAs are allowed, they will be contingent on investment performance rather than an automatic CPI-related formula;
- The schedule to amortize the reduced UAAL will be re-amortized to 25 years from the current 19-year schedule, which will not reduce the UAAL, but will reduce the annual contributions, although increasing the total pension payments over time.

The draft actuarial report for June 30, 2011 indicates that the system's UAAL decreased from \$6.87 billion to \$4.38 billion. Rhode Island has full or partial funding responsibilities for the state employees, teachers, judges, and state police systems, and the funding ratio improved to 59% from 48%. The UAAL for the MERS plan for local municipalities was also significantly improved, and the annual required contributions for both state government and local governments will be reduced beginning in fiscal 2013. Furthermore, the actuarial analysis indicates that the fiscal 2013 required pension contributions by local governments for municipal and public safety employees and teachers will decline by \$110 million, or almost 40%. Officials indicate that the pension funding savings for the state government in fiscal 2013, including the state's share of teacher contributions will be about \$240 million.

The unfunded liability for the state's other post employment benefits, as of June 30, 2011 (the latest valuation), was \$866.3 million, a \$91 million increase from the 2009 valuation. The liability is about \$820 per capita. Rhode Island budgeted for the full OPEB ARC in fiscals 2011 and 2012, and began funding its OPEB trust fund during 2011.

On a four-point scale on which '1' is the strongest, we have assigned a '2.4' to Rhode Island's debt and liability profile.

Related Criteria And Research

- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- USPF Criteria: Moral Obligation Bonds, June 27, 2006
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

Ratings Detail (As Of April 20, 2012)		
Rhode Island & Providence Plantations COPs		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
Rhode Island & Providence Plantations COPs (ASSURED GTY)		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
Rhode Island & Providence Plantations GO (FGIC)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Rhode Island & Providence Plantations GO (MBIA) (AMBAC)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Rhode Island & Providence Plantations (Energy Conservation Proj)		
<i>Long Term Rating</i>	AA-/Stable	Affirmed

Rhode Island & Providence Plantations; Appropriations; General Obligation; Moral Obligation

Ratings Detail (As Of April 20, 2012) (cont.)

Rhode Island & Providence Plantations (Info Technol Proj) (ASSURED GTY)

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island Convention Ctr Auth fixed rate rev

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island Convention Ctr Auth rev

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island & Providence Plantations Ise part certs (Shepard's Bldg) rfdg ser 2007F

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island & Providence Plantations Ise part certs 2005 ser C (Training Sch Proj)

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island & Providence Plantations Ise (Correctional Facs) 1997

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island & Providence Plantations GO

Unenhanced Rating AA(SPUR)/Stable Affirmed

Rhode Island Convention Ctr Auth, Rhode Island

Rhode Island & Providence Plantations, Rhode Island

Rhode Island Convention Ctr Auth (Rhode Island & Providence Plantations)

Long Term Rating AA-/Stable Affirmed

Rhode Island Convention Ctr Auth (Rhode Island & Providence Plantations) (ASSURED GTY)

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Rhode Island Econ Dev Corp, Rhode Island

Rhode Island & Providence Plantations, Rhode Island

Rhode Island Econ Dev Corp (Rhode Island & Providence Plantations)

Long Term Rating AA-/Stable Affirmed

Rhode Island Econ Dev Corp (Rhode Island & Providence Plantations) (38 Studios, Lic Proj) (AGM)

Unenhanced Rating A(SPUR)/Stable Affirmed

Rhode Island Econ Dev Corp (Rhode Island & Providence Plantation) taxable econ dev rev (FMR Rhode Island Inc. Proj)

Long Term Rating A/Stable Affirmed

Many issues are enhanced by bond insurance.

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MOODY'S

INVESTORS SERVICE

New Issue: MOODY'S ASSIGNS Aa2 RATING TO RHODE ISLAND'S APPROXIMATELY \$125 MILLION GENERAL OBLIGATION REFUNDING BONDS; OUTLOOK REMAINS NEGATIVE

Global Credit Research - 19 Apr 2012

STATE HAS \$2.1 BILLION IN NET TAX-SUPPORTED DEBT OUTSTANDING

RHODE ISLAND (STATE OF)
State Governments (including Puerto Rico and US Territories)
RI

Moody's Rating

ISSUE	RATING
Consolidated Capital Development Loan of 2012, Refunding Series A	Aa2
Sale Amount	\$125,000,000
Expected Sale Date	05/01/12
Rating Description	General Obligation

Moody's Outlook N/A

Opinion

NEW YORK, April 19, 2012 –Moody's Investors Service has assigned a Aa2 rating to the State of Rhode Island's General Obligation Bonds, Consolidated Capital Development Loan of 2012, Refunding Series A. The bonds, which are expected to price the week of April 23rd, include about \$64 million of general obligation refunding bonds, \$42 million of transportation refunding bonds, and \$20 million in transportation restructuring bonds. The state anticipates net present value savings of about \$8 million from the transaction.

SUMMARY RATING RATIONALE

The Aa2 general obligation rating incorporates Rhode Island's institutionalized governance practices; maintenance of modest but positive general fund balances, including a fully funded budget reserve fund (BRF); narrow liquidity; and an economy that has long lagged the nation's. The rating reflects the state's persistent revenue under-performance and spending challenges; its record of balancing budgets with one-time solutions; and a history of substantial short-term borrowings for cash flow purposes.

Credit strengths:

*Institutionalized governance practices such as bi-annual consensus revenue estimating conferences and out year budget planning

*History of funding budget reserve fund at constitutional cap

* Wide legal powers--similar to other state governments--to raise revenue and adjust spending in order to maintain fiscal solvency.

Credit challenges:

*Consecutive budget gaps for fiscal years 2007 through 2011, and forecast for fiscal 2012, due to revenue underperformance and continuing spending pressures

*Past reliance on one-time budget solutions contributes to recurring budget shortfalls

*Consecutive years of cash flow borrowing and slim cash margins underscore state's slim liquidity

*Long-term economic underperformance with meager long-term employment growth rates and very high unemployment rates.

*Pending litigation challenging constitutionality of pension reforms

DETAILED CREDIT DISCUSSION

BOND DEAL REFLECTS GOVERNOR'S INITIATIVE TO PROVIDE RELIEF TO DEPARTMENT OF TRANSPORTATION

Although the bulk of the Series 2012 bonds provide annual debt service savings and maintain existing maturities, the \$20 million in transportation restructuring bonds extends final maturities from fiscal 2015 to fiscal 2028. The restructuring bonds provide upfront cash flow savings of nearly \$10 million in fiscal 2013 and another \$10 million spread between fiscal 2014 and 2015, and on net result in present value dis-savings of about \$900,000. The governor has announced his intention to improve liquidity in the state department of transportation by reducing debt service in the near term and to provide additional funds for pay-as-you-go capital spending by accelerating a fee increase approved in the 2011 legislative session. The General Assembly has already approved a plan to transfer responsibility for departmental debt service to the general fund in \$10 million annual increments. The phase-in is expected to be completed by fiscal 2018, resulting in additional general fund debt service expense of \$45 million.

REVENUES TICK UP IN STAGNANT ECONOMY

Rhode Island's November 2011 revenue estimating conference (REC) projected a 3.6% increase in fiscal 2012 revenues from fiscal 2011 collections. The projection was a slight improvement from the enacted budget's forecast for 3% growth. Actual collections have run ahead of the November forecast, with fiscal year-to-date revenues exceeding the forecast by \$63 million. However, uncertainty regarding the pattern of final payments for personal income taxes following changes in the tax code enacted in the 2010 legislative session, effective January 1 2011, has led state budget officials to caution that the excess collections could be partially erased in April.

State economic trends do not augur well for tax collections, as payroll employment has failed to grow with the nation's economic recovery. Total payroll employment stood at 458,000 jobs in February, roughly level with the job count in the spring of 2010. The unemployment rate has also failed to improve, hovering near or above 11% since July 2009.

FISCAL 2013 BUDGET PROPOSAL SEEKS REVENUE BASE EXPANSION

Governor Chafee's proposed fiscal 2013 budget seeks to close an estimated \$166 million budget gap and increase education funding through a mix of revenue increases and expenditure cuts. Last year, the governor attempted to implement significant changes to the state's sales tax through base broadening and rate changes, which were largely rejected by the state legislature. This year's proposal is more modest, with sales tax base broadening targeted at a handful of services and removal of an exemption for sales of clothing costing more than \$175 per item. In addition, the proposed budget would increase the meals and beverage tax, the proceeds from which would fund a portion of the governor's initiative to fully fund a new education formula, and a lodging tax. The revenue proposals, which also include a one-time tax amnesty program and appropriation of a bond premium, would raise about \$90 million. This amount would be roughly matched by expenditure reductions.

The governor's budget is notable in that it attempts to address the fiscal 2013 budget gap with only \$20 million in one-time revenue actions. In previous years the state has relied heavily on one-time actions to achieve budget balance. Nonetheless, the proposed budget balances fiscal 2013 by a very narrow margin. The year-end budgetary balance is projected to be just \$1.4 million, less than one-half of one percent of the state's general fund revenues. The projected closing balance for fiscal 2012 is also slim at \$5.8 million.

BUDGET GAPS REMAIN A CHALLENGE

Although the projected budget gaps the state has had to close have diminished with the improvement in the national economy, budget shortfalls continue to challenge state finances. Projected budget gaps as a percent of general fund revenues fell from 18% in fiscal 2010 to 15% of general fund revenues in fiscal 2011 and 10% of revenues in fiscal 2012. The fiscal 2013 gap as projected in the governor's proposed budget is about 6% of general fund revenues,

once the impacts of pension reforms passed in the fall of 2011 are accounted for. However, the governor's five-year forecast projects budget shortfalls that grow to \$325 million by fiscal 2017. After accounting for the estimated negative impacts on gaming revenues of recently-enacted expansion of gaming operations in Massachusetts, the governor's projected budget shortfall grows to \$464 million in fiscal 2017.

MANDATORY FUNDING OF BUDGET RESERVE IMPROVES FUND BALANCES AND LIQUIDITY

Rhode Island's constitution requires the state to appropriate less than projected revenues to fund a budget reserve account (BRF). This requirement was strengthened by a 2006 constitutional change increasing the BRF cap from 3% of revenues to 5%. The new cap will be phased in by 2013. If the BRF is fully funded, excess revenues flow into a capital account (RICAP). The constitutional change also restricted the use of this fund to capital purposes.

Despite its fiscal distress, Rhode Island maintained positive available fund balances throughout the recent recession. Fund balances reached a low of 0.6% of revenues in 2009 but rebounded to 4.3% of revenues in fiscal 2011.

The state has relied on cash flow notes to maintain liquidity, issuing \$120 million in cash flow notes in fiscal year 2007, \$220 million in fiscal year 2008 and \$350 million in fiscal years 2009, 2010, and 2011 due to further tightening of cash flow margins. The state borrowed less in fiscal 2012, reducing its cash flow notes to \$200 million. The state has not yet tapped the cash flow note proceeds, an indication of Rhode Island's improving liquidity position.

LONG-RUN IMPROVEMENT IN STATE'S DEBT BURDEN CHALLENGED BY HIGHWAY NEEDS

Rhode Island's debt burden has dropped considerably over the past 10 years, although the state's debt ratios remain above average. Total tax-supported debt in fiscal 2011 was \$2.1 billion, a decline from the fiscal 2010 level of \$2.3 billion. Fiscal 2011's decline in debt outstanding occurred after five consecutive years of increase. In Moody's 2011 debt medians report, Rhode Island's net tax-supported debt was 5.3% of total state personal income, ranking it 13th in the nation, down two notches from 2010. While still notably higher than Moody's 2010 50-state median of 2.8%, Rhode Island's debt burden remains well below the near-9% level the state experienced in the early 1990s. Rhode Island's debt per capita ranked 10th in 2011 at \$2,191, a notch lower than 2010. The 2011 median debt per capita for states was \$1,066. The long-run improvement in debt ratios reflect deliberate debt reduction policies, increased pay-as-you-go capital funding, as well as gains in personal income. The increase in the state's debt ratios in the last several years stems primarily from debt issued to fund highway capital projects. Rhode Island has funded nearly all of its highway-related capital program with debt. In the 2011 legislative session, the General Assembly increased fees to reduce the highway program's debt-dependency.

MAJOR REFORM OF STATE PENSION SYSTEM INCREASES FUNDED STATUS; RAISES QUESTIONS

In November 2011, the General Assembly passed legislation to overhaul the state's pension system. Rhode Island's reported pension funded ratio (the ratio of the actuarial value of assets to actuarial accrued liabilities) had been among the lowest of the states, measuring 61% in fiscal 2009. The state's low funded ratio persisted despite the state annually contributing the full amount of its actuarial required contribution. After changing certain actuarial assumptions and methods in the spring of 2011, the funded ratio plummeted to 48%. (For a more detailed discussion of the changes to Rhode Island's actuarial assumptions, please refer to our May 31, 2011 issuer report).

The most significant portion of the reform package creates a hybrid system that combines a reduced defined benefit augmented by a 401(k)-style defined contribution system. Automatic cost-of-living adjustments are suspended until the system reaches an 80% funded level, but interim adjustments will be allowed at five-year intervals, depending on investment performance. Unlike reforms many states have enacted that apply only to future employees, certain changes in the Rhode Island reform, such as retirement eligibility ages, will apply to current employees while reduced cost-of-living adjustments will apply to current retirees.

The reform reduced the state's fiscal 2013 general fund pension contribution from a projected \$305 million to \$177 million, according to General Assembly documents. The state reports that the changes increased the system's funded ratio from 48% to 59%.

Unions representing public sector employees have sued to challenge the constitutionality of previous reforms enacted by the Rhode Island General Assembly, and while no lawsuit has yet been filed in reaction to the most recent set of reforms, the state anticipates that additional litigation will be pursued by employee representatives. A lower court decision held that pension benefits constitute a contractual agreement between the state, and the state is continuing to pursue its options to contest the lawsuit. Some other states' pension reform packages have been

successfully challenged on the basis of constitutional protections of contractual agreements, although this principal has not prevailed in every case.

MINIMAL OPEB LIABILITY HELPS MITIGATE HIGH DEBT AND PENSION BURDEN

Rhode Island's unfunded liability for other post employment benefit costs (OPEB) is estimated at approximately \$822 million as of June 30, 2009. This amount includes \$674 million for state employees, \$67 million for state police, \$12 million for legislators, \$9 million for judges, and \$14 million for the state's share of teacher's OPEB costs. The state funded its OPEB obligation until fiscal year 2010 on a pay-go basis for current benefits to retirees but began funding OPEB on an actuarial basis in fiscal year 2011. Its FY 2011 OPEB ARC payment was a manageable \$53 million, about 1.8% of revenues.

Outlook

The negative outlook reflects the state's narrow liquidity margins, below-average economic performance and persistent budget gaps. While the pension reforms enacted in the fall of 2011 remove some budgetary pressure, the legal status of those reforms remains unsettled. A court decision against the state could result in significant costs.

What would make the rating move - UP

- *Maintenance of stronger reserve levels
- *Sustained economic improvement at least in line with national average based on various metrics including job growth
- *Restoration and maintenance of structural budget balance
- *Resolution of pension-related litigation in the state's favor

What could change the rating - DOWN

- *Mounting combined debt and pension liability burdens with no plan to address them
- *Deterioration of state's reserve and balance sheet position
- * Persistent economic weakness indicated by lack of employment recovery when the rest of the nation rebounds
- *Increased liquidity pressure reflected in narrower cash margins, increased cash flow borrowing, or a shift toward tactics such as delayed vendor or other payments to gain short-term liquidity relief
- *Continued significant reliance on one-time budget solutions, particularly deficit financing
- *Resolution of pension litigation in employees' favor

PRINCIPAL RATING METHODOLOGY

The principal methodology used in this rating was Moody's State Rating Methodology published in November 2004. Please see the Credit Policy page on www.moody.com for a copy of this methodology.

REGULATORY DISCLOSURES

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FitchRatings

FITCH RATES RHODE ISLAND'S \$96MM GO BONDS 'AA'; OUTLOOK STABLE

Fitch Ratings-New York-18 April 2012: Fitch Ratings assigns an 'AA' rating to the State of Rhode Island and Providence Plantations' general obligation (GO) bonds consisting of:

--\$96.35 million consolidated capital development loan of 2012, refunding series A.

The bonds are expected to sell via negotiation the week of April 23, 2012.

In addition, Fitch affirms the following ratings:

--\$1.19 billion in outstanding state GO bonds at 'AA';

--\$733.6 million in outstanding appropriation-backed debt at 'AA-'.

The Rating Outlook is Stable.

SECURITY

The bonds are general obligations of the State of Rhode Island and Providence Plantations, secured by a pledge of the state's full faith and credit.

KEY RATING DRIVERS

IMPROVED FINANCIAL PERFORMANCE: State-source revenues, particularly sales and personal income taxes, have shown notable improvement in fiscal years 2011 and 2012. The state added to its rainy day fund in 2011 and expects a further addition in 2012.

STRONG FISCAL MANAGEMENT: The state's financial operations are conservatively managed and the state acts proactively to close budget gaps through primarily structural solutions. Additionally, in fiscal 2013 the state will reach its constitutionally mandated targets of limiting budget appropriations to 97% of estimated revenue and maintaining 5% in its budget reserve account.

SIGNIFICANT PENSION REFORM HAS STABILIZED LIABILITY POSITION: The state's comprehensive reform of its pension systems has significantly improved funded ratios while lowering annually required contributions. The state's debt position remains above average.

SLUGGISH ECONOMY WITH HIGH UNEMPLOYMENT: Economic tailwinds in early 2011 trailed off toward the balance, with small job losses continuing into 2012. High unemployment rates have stabilized, but this is partly due to a falloff in the labor force. Employment gains are expected to be slow over the next several years.

CREDIT PROFILE

The state's 'AA' GO bond rating is based on improved financial performance, conservative fiscal management, and a manageable debt position, offset by economic performance that continues to be among the weakest in the nation with lackluster employment growth anticipated in future years. After adding jobs every year from 1992 through 2006, the state fell into the recession early, with year-over-year (YOY) job losses beginning in August 2007. Rhode Island's unemployment rate reached 11.9% in January 2010; the rate in February 2012 was 11%, pointing to continued economic weakness.

These fragile economic conditions and a struggling real estate market pressured state revenues in

the recession and challenged fiscal health and stability, severely straining the state's financial position. However, despite continued economic weakness, the state's financial position has shown recent improvement, boosted by growth in economically sensitive revenue sources, allowing the state to add to its rainy day fund in fiscal 2011 with a further addition expected in fiscal 2012.

SLUGGISH ECONOMIC PERFORMANCE

While the state's economy has stabilized from its prior freefall position, current economic indicators point to an economy that will be slow to recapture employment lost in the recession. The 11% unemployment rate in February 2012, second highest in the nation and notably higher than the 8.3% national average, has approximated this average since mid-2009 and the Global Insights economic forecast does not predict a return to pre-recession employment levels until 2020, the slowest of the states. Further, the state continues to shed active participants in the labor force as the number of residents in the labor force has steadily fallen since April 2010.

In February 2012, the state recorded YOY employment loss of 0.2% as compared to 1.6% growth for the U.S. The most notable losses were in the other services (down 6.5%), construction (3.8%), and leisure and hospitality (2.8%) sectors. These losses were somewhat offset by improvement in information, manufacturing and professional, business, education, and health services. The weak employment picture continues to hamper recovery in the state's real estate market, which suffered from a steep market correction in the national housing downturn. Housing prices are anticipated by Global Insights to bottom out in 2012 and begin to improve in 2013 while housing starts are expected to increase in 2012 and remain strong but at a much reduced rate than pre-recession.

IMPROVED FINANCIAL POSITION

Despite the damp economic picture, economically sensitive revenue sources have rebounded, improving financial margins and providing the state the opportunity to add to its reserves. The state's finances felt the effects of the recession early, with revenue declines beginning as early as November 2007. Fiscal 2008 closed with a deficit of approximately \$43 million, even after deficit financing in the form of tobacco settlement bonds, and the state grappled with multiple rounds of budget gaps in fiscal 2009. At the close of fiscal 2009, the state's budget reserve carried a balance of \$80 million, equal to 2.7% of revenues, which the state was able to increase to \$112 million in fiscal 2010, the maximum allowed by law.

A budget gap of \$427 million was estimated for fiscal 2011 and was subsequently closed through local aid and school cuts, federal stimulus funds from two additional quarters of enhanced FMAP, savings from the prior year's pension reform, and an increase in hospital license fees. Fiscal 2011 ending with a GAAP basis operating surplus of \$85 million and an \$80.7 million deposit to the Budget Reserve Fund (BRF), increasing total rainy day funds to \$130 million.

An early estimated budget gap of \$295 million for fiscal 2012 was largely addressed in the governor's proposed budget through structural budget solutions, encompassing both revenue enhancements and expenditure modifications, consistent with the state's well managed financial operations. Surplus revenue from fiscal 2011 of \$57.2 million was rolled into fiscal 2012, and when combined with \$66.7 million of increased revenue forecast for fiscal 2012, reduced the expected gap to \$171 million. To close the remaining gap, the legislature extended sales taxes to additional items, increased various user fees, increased the hospital licensing fee, and cut social services spending and spending in other departments. The state also planned for a \$90.5 million addition to its rainy day fund at fiscal year-end.

The state Revenue Estimating Conference (REC) revised its revenue forecast for fiscal 2012 in November 2011 upwards by \$19.4 million (3.6% growth from fiscal 2011 audited results) from the final enacted total of \$3.176 billion. Based on the constitutional funding formula that calculates contributions to the BRF, which limits annual appropriations to 97.2% of estimated revenues in fiscal 2012, another deposit of \$91.4 million is estimated to be made in fiscal 2012.

Actual adjusted general revenue through March 2012 is running \$62.5 million or 3% higher than the revised November 2011 estimate and actual cash collections are 3.7% better YOY as compared to fiscal 2011. Personal income tax receipts (PIT) compare favorably to fiscal 2011 with a 6.4% YOY increase and are 3.9% above estimate. Sales tax receipts are also up YOY at 4% growth that

is essentially meeting estimates, however, these results partly reflect an expansion of the sales tax base that was effective in October 2011. Currently, the state anticipates ending fiscal 2012 with a larger operating surplus than was forecast by the REC.

Prior to the passage of the state's comprehensive pension reform in the fall of 2011 and the November REC, a budget gap of \$214.8 million was forecast for fiscal 2013, which begins on July 1. The gap was based on the maintenance of current service levels, required contribution increases to the pension systems, and fully funding the state education funding formula. The fall pension reform, which provided about \$117 million in budget relief for fiscal 2013, together with a reduction in agency requests less \$19 million in weaker expected revenues, reduced the forecast budget gap to \$165.7 million.

The governor's recommended fiscal 2013 budget estimated general revenues of \$3.366 billion, comprised of \$3.129 billion of revenue estimated at the November 2011 REC (a 3% YOY increase), \$143.8 million from maintaining the hospital license fee, and \$92.9 million from proposed revenue enhancements. Revenue proposals include expanding the sales tax base to include four previously exempt services; increasing the beverage and meals tax; and increasing the cigarette tax. These revenue enhancements are proposed to not only close the expected budget gap but also fully fund and augment education funding, provide additional local aid, address the structural deficit at the department of transportation, and implement various agency initiatives. The budget proposal is still being considered by the legislature with budget adoption expected in the late spring.

ABOVE AVERAGE BUT STABILIZED LIABILITY BURDEN

Prior to significant recent reforms, the state's liability position was characterized by notably low pension funding levels (48.4% as of June 30, 2010). The state undertook two rounds of pension reform in 2011; in the first round, the state made a variety of conservative adjustments, including reducing the return assumption to 7.5% from 8.25%, reducing the rate of inflation, and increasing the life expectancy of retirees, which raised the state's unfunded actuarially accrued liability (UAAL). In late 2011, a second round of reform included establishing a hybrid defined benefit-defined contribution system and making future cost-of-living adjustments (COLAs) contingent on investment performance and the funded level of the plan.

The latter round of changes improved the funded ratios and lowered the plan's forecast contributions considerably. The UAAL for state employees (ERS) based on the June 30, 2010 valuation dropped to \$1.7 billion from \$2.7 billion; for teachers (TRS), the UAAL fell to \$2.4 billion from \$4.1 billion. For fiscal 2011, based on the noted pension reforms, the ERS funded ratio increased to 59.8%; TRS funding increased to 61.8%. The systems are expected to reach 80% funded in 2032 for ERS and 2020 for TRS with full funding of the systems expected in 2035.

Rhode Island's debt ratios are on the high end of the moderate range, with net tax-supported debt of \$2.4 billion equal to about 5.2% of personal income compared to the 2.9% median for states rated by Fitch. The state has made a concerted effort to reduce debt levels although issuance increased in fiscal 2009 with debt for transportation programs and bonding for the state's historic structures tax credit liability to provide budget relief. The current series A bond offering is a refunding for debt service savings although the governor has introduced a November 2012 ballot proposal totaling \$201 million for various capital projects including construction of a nursing center at the University of Rhode Island, capital improvements at the Rhode Island College, and transportation, clean water, affordable housing, and open space projects.

On a combined basis, the burden of the state's net tax-supported debt and adjusted unfunded pension obligations equals 11.7% of 2011 preliminary personal income, well above the 6.6% median for U.S. states rated by Fitch. The calculations include 100% of the liability of ERS and the 40% of the TRS liability for which the state is responsible.

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In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from IHS Global Insight.

Applicable Criteria and Related Research:

- 'Tax-Supported Rating Criteria', dated Aug. 15, 2011;
- 'U.S. State Government Tax-Supported Rating Criteria', dated Aug. 15, 2011;
- 'Improving Comparability of State Liabilities' dated March 28, 2012;
- 'Fitch: Effect of Sweeping Rhode Island Pension Reform May Be Felt Nationwide' dated Nov. 17, 2011.

Applicable Criteria and Related Research:

Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=648898

U.S. State Government Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=648897

Improving Comparability of State Liabilities

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