

RatingsDirect®

University Of Maine System; Public Coll/Univ - Unlimited Student Fees

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Credit Profile

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<i>Long Term Rating</i>	AA-/Stable	Affirmed
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<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rating Action

S&P Global Ratings' affirmed its 'AA-' long-term rating and underlying rating (SPUR) on University of Maine System's (UMS or the system) various series of revenue bonds outstanding. The outlook is stable.

A broad pledge of the system's available revenue, which include tuition, fees, and charges for its educational services as well as its auxiliary enterprises together with other available monies, secures the bonds. We understand the system could issue additional debt later this year for a new engineering building on the flagship campus. We also understand that the state intends to partially support debt service associated with the issue in the total amount of \$50 million over a 10-year period.

As a result of the COVID-19 pandemic, UMS transitioned all undergraduate and course instruction to an online format effective the week of March 23 through the remainder of the academic year as well as for the summer sessions. Most students have vacated the campus, with those remaining subject to social-distancing measures and reduced on-campus services. Most faculty and staff, including non-essential research, have transitioned to remote work. Given the uncertainty of the virus' duration, there is no timetable for when instruction, research and campus operations will return to normal. The university expects the primary impact for fiscal 2020 will be a loss of revenue from pro rata refunds on room and board for students who have left campus. Management expects these losses will be offset by some expense savings as non-discretionary spending and hiring slow. In our view, the full financial impact of COVID-19 cannot be quantified at this time, but we believe for fiscal 2020 it will affect UMS' operating results, with weaker results than fiscal 2019 expected. UMS was allocated \$17.3 million under the CARES Act, of which half or \$8.6 million will be available to the system to blunt the COVID-19 impact. Fiscal 2021 performance could be more severely impaired, depending upon the trajectory of the virus and its effect on operations. We recognize that UMS has taken prudent measures to address the current situation and the system continues to monitor the course of the pandemic,

having fully evaluated additional measures that the system could take to protect the health of the community and promote its core mission of academics and research. We believe UMS' healthy balance-sheet strength and liquid resources will help the institution offset medium-term pressure that might arise as a result of the pandemic. UMS indicates that its operating portfolio at Feb. 29, 2020, had \$331 million of assets of which 89% or \$295 million can be liquidated on a daily basis with remaining amounts that could be liquidated in 30-90 days.

Credit overview

We assessed UMS' enterprise profile as strong characterized by its breadth and depth, including the state's land-grant and flagship higher educational institution, University of Maine (located in Orono), together with six other universities and other educational sites located in various parts of the state. UMS' stable demand, with total fall 2019 full-time equivalent (FTE) enrollment of 21,924, essentially the same enrollment it realized in the previous year. Unfavorable demographics for Maine college-bound high school seniors and strong regional competition continue to present challenges for enrollment growth and are exacerbated by the current coronavirus pandemic and uncertainty surrounding the opening of school for fall 2020. The various campuses operate under a common system, governance, and we view management as satisfactory, augmented by direct state oversight for certain functions; the system's debt outstanding is limited by state statute to \$350 million.

We assessed UMS' financial profile as very strong, recognizing its healthy financial management policies, sound financial performance, robust financial resources, and low debt and contingent liabilities. Also, UMS' debt amortization is shorter than most colleges and universities as its various bond issues have a maximum initial term of 20 years compared with the more typical 30-year amortization period. Combined, we believe these credit factors lead to an indicative standalone credit profile of 'a+'. As our criteria indicate the final rating can be within one notch of the indicative credit level. In our opinion the 'AA-' rating on the system's bonds better reflects the strength of UMS' financial resources and low debt for the rating category relative to medians and peer institutions.

The ratings and outlook also reflect our view of the system's:

- Positive cash-based adjusted operating surpluses in each of the past five audited fiscal years ended June 30, 2019, while full accrual-based adjusted operating margins are more volatile and sometimes negative;
- Sound revenue diversity with tuition and fees accounting for 38% of adjusted operating revenue followed by state operating appropriations at 26%, grants and contracts at 17%, and auxiliary operations at 10% and 9% miscellaneous, including investment income and gifts;
- Increasing state operating appropriation and limited capital support from state-authorized and issued borrowing that doesn't require reimbursement from the system for debt service;
- Healthy available resources for the rating with fiscal 2019 adjusted unrestricted net assets to debt outstanding of 147.9%, although adjusted unrestricted net assets (UNA) are less favorable on an adjusted operating expense basis at 24.8%;
- Manageable debt and contingent liabilities, with a low debt burden and all fixed-rate debt, no interest-rate swaps, or risks associated with direct placement debt; and
- Satisfactory governance and management that employs conservative budgeting practices and imparts fiscal discipline through using dashboard indicators and long-term financial planning.

These credit strengths are diminished by our view of the system's:

- Unfavorable demographic statistics for college-bound high school graduating seniors that will continue to make growing enrollment difficult;
- Underused physical capacity among over 550 buildings aggregating in excess of 9 million square feet of space that system management acknowledges is cost inefficient, with an ongoing plan that is slowly making progress in razing outdated buildings; and
- Ongoing budgetary deficits before adjustments for reserve utilization and incorporation of anticipated cost savings, i.e. items that we consider non-recurring, to close deficits.

The stable outlook reflects our view that UMS' enrollment will remain relatively stable while recognizing that the COVID-19 pandemic presents real risk if the campuses can't be opened fully in fall 2020. In addition, we believe management and governance will continue to provide leadership during these difficult times such that ongoing operations will be closely monitored and needed adjustments made in a timely fashion to maintain the system's robust financial resources and low debt that provide some flexibility to deal with the unexpected. The stable outlook also assumes that the state's commitment to the system will not decline materially.

UMS' seven universities, some with multiple campuses, include the flagship University of Maine in Orono that is about 10 miles north of Bangor, and about 137 miles northeast of Portland. The University of Maine System was created by the Maine Legislature in 1968 through the merger of the University of Maine--which consisted of a main campus in Orono, a law school in Portland, and branch campuses in Augusta and Portland--with Maine's five state colleges.

Maine's economy is relatively diverse, although long-term economic growth prospects are challenged by the state's demographic profile and by wealth and income levels that are below that of the nation. In our view, the declining demographic for Maine high school seniors, combined with limited job opportunities for college graduates and significant competition from New England peer institutions, together with the COVID-19 impact presents the system with a difficult course to navigate over the next two years. We understand, however, a system initiative to attract out-of-state students by offering tuition comparable with the student's home state tuition rate has shown signs of success and helped maintain a relatively stable freshman class size.

Environmental, social, and governance factors

In our view higher education entities face elevated social risk due to the uncertainty on the duration of the COVID-19 pandemic, and unknown impact on fall 2020 enrollment levels and mode of instruction. We view the risks posed by COVID-19 to public health and safety as a social risk under our environmental, social, and governance (ESG) factors. Despite the elevated social risk, we believe UMS' environment and governance risk are in line with our view of the sector as a whole.

Stable Two-Year Outlook

Downside scenario

A lower rating is possible if the pandemic adversely affects fall 2020 enrollment resulting in a spike in UMS' full-accrual based operating deficit such that financial resources decline to a level no longer consistent with the rating category. In

addition, any material diminution in state support or significant increase in debt without a commensurate increase in available resources could trigger a lower rating. In light of coronavirus challenges, we believe the system will make limited progress in addressing its deferred capital maintenance needs over the next two years as it seeks to preserve its financial resources.

Upside scenario

A higher rating is not a consideration at this time, because of the uncertainty about the coronavirus pandemic as well as the state's current fragile economy, coupled with unfavorable high-school-age demographics and brisk competition among New England-based schools for students. A higher rating is possible if UMS' enrollment grows and is sustained while financial performance becomes stronger and financial resources grow sufficiently to offset the impact of any additional debt issuance should that become necessary.

Credit Opinion

Enterprise Profile

Industry risk

Industry risk addresses the higher education sector's overall cyclical, competitive risk, and growth by applying various stress scenarios and evaluating barriers to entry, levels and trends of profitability, substitution risk, and growth trends observed in the industry. We believe the higher education sector represents a low credit risk when compared with other industries and sectors.

Economic fundamentals

In our view, UMS' good geographic diversity is limited, with Maine residents accounting for approximately 86.1% of the total fall 2019 enrollment for all campuses. Therefore, our assessment of UMS' economic fundamentals is anchored by the Maine GDP per capita of \$49,765, which is below the national GDP of \$64,670.

Market position and demand

UMS' enrollment continues to feel the effect of the state's slow long-term growth trend and its unfavorable high-school-age demographic. After a small increase in FTE enrollment in fall 2018, it decreased 0.5%, for the third time in five years, to 21,924 in fall 2019 from 22,033 in 2018. Freshman applications, however, have increased in four of the past five years, and increased 10.9% to 26,614 in fall 2019 from the previous year. The acceptance rate for the past five fall enrollment periods averaged 79% with little deviation. The fall 2019 acceptance rate was 77.8%. Matriculation is low, in our view, and was 20.8% in fall 2019. We believe enrollment for most colleges and universities in the northeast will remain pressured for the near term due to increasing competition for a dwindling supply of high school graduating seniors.

Student quality, as measured by the SATs at 1068 for fall 2019, has been relatively static and slightly below that of New England peers, and slightly below the national average in recent years. We understand historical freshman-to-sophomore retention rates are typically in the low-70% range, and the retention rate was 73% in fall 2019. Tuition and mandatory fees are among the lowest for in-state and out-of-state students, compared with those of other

New England schools. Furthermore, UMS reports that the system has the lowest room and board fees of its New England peers. The tuition is \$7,872 for in-state students and \$17,976 for out-of-state students; both are lower than UMS' regional peers. The overall average tuition increase for fall 2017 was 2.8% for both undergraduate in-state and undergraduate out-of-state students. The system commissioned a pricing, marketing, and financial study that identified several strategies to attract and retain students. Some of these include attracting international, out-of-state, and in-state college-bound high school students. About 80% of the undergraduate student enrollment comes from in-state residents, which is in line with the past two years. The state aims to raise postsecondary participation rates by requiring all high school juniors take SATs, and strongly encourages these students to apply to at least one college or university.

Governance and management

UMS is led by its chancellor, Mr. Dannel P. Malloy, who assumed the position in July 2019. Mr. Malloy is the former governor of Connecticut. On July 1, 2018, Ms. Joan Ferrini-Mundy, Ph.D., became the new president of the flagship campus and University of Maine at Machias. Ms. Ferrini-Mundy comes to Maine from the National Science Foundation where she was the chief operating officer. We believe these recent changes should strengthen the system's governance and management.

The system continues to implement the strategic plan it adopted in January 2012, which was last updated in 2014 and is currently being refined. The plan's four major focus areas are:

- Increasing enrollment;
- Promoting student success;
- Achieving fiscal sustainability; and
- Realizing improved economic development within the state by expanding research.

The system's "One University for all of Maine" initiative, launched by former Chancellor James Page, has evolved now with the System Board's January 2020 approval to pursue a unified accreditation for the system, covering all of its universities, from its regional accreditor, the New England Commission of Higher Education. Unified accreditation will permit greater academic collaboration between system universities so that two or more universities can coordinate to offer academic programming that any one university does not have sufficient resources to offer on its own. The system expects to realize significant academic and financial efficiencies while preserving academic programs necessary to meet its statewide mission.

In our view, the system has a high level of deferred capital maintenance owing to the age of its infrastructure and its practice of not fully funding depreciation costs, although it has a goal to reach 100% by fiscal 2024, and budgeted at 66% and 75% for fiscal years 2020 and 2021, respectively. We understand that just over half of the system's buildings are approximately 50 years old. The state legislature sent a \$49 million bond referendum to voters in Nov. 2018 that was approved for modernizing and improving facilities and infrastructure of the university. In March 2020, the system obtained board authorization to proceed with three projects on the Portland campus of the University of Southern Maine. These projects include a student residence hall, a parking facility, and a career and student success center.

We understand labor relations have generally been stable, with six collective bargaining units representing various

classes of workers.

Financial Profile

Financial management policies

UMS annually produces independently audited full-accrual financial statements that have not had any qualifications. Modified accrual budget-to-actual financial reports are presented to each university's chief budget officer monthly. In addition, management reports interim financial results as of the end of March and the system updates its current-year forecast in October, February, and April based on current financial data. In our view, credit weaknesses are recurring budgetary deficits that grow considerably larger in out-year forecasts and the practice of not yet fully budgeting for depreciation.

Cash and debt management functions are centralized at the system. While UMS does not have a formal written policy specifying a minimum required reserve and/or liquidity balance, it does have an administrative practice letter that was approved on July 1, 2017, that establishes target levels for operating and other reserve balances. In addition, it has written and board approved policies for investment and debt management that it routinely follows and that we deem a best practice.

Financial performance

UMS' recorded full-accrual based adjusted operating deficits for fiscal 2018 and 2019. For fiscal 2019 on an adjusted full-accrual operating basis the deficit is approximately \$16.9 million or 2.0% of total adjusted operating expenses. The key drivers affecting financial operating performance on a full-accrual basis in fiscal 2019 are a very slight decline (0.5%) in the FTE enrollment trend, modest 2.7% increase in tuition and total operating expense year over year growth of 4.6% up from 3.6% in the prior year. On a cash basis, the system has been profitable in all years.

UMS' revenue stream remains diverse, with fiscal 2019 operating revenues split approximately three ways: 37.8% of revenues from student-related fees and tuition, 25.6% from state appropriations, and 16.8% from grants and contracts; the remaining 20% representing auxiliary operations and other miscellaneous revenue sources.

In our view, the state's support for higher education funding in comparison with other states is fairly good, with modest year-over-year increases in appropriation realized in most recent years. Revenue from state appropriation realized in fiscal 2019 totaled \$211.98 million up 0.5% from the previous year's \$210.98 million. A slightly higher increase should be realized for fiscal 2020 and continuation of that trend expected for fiscal 2021. Also, Maine voters authorized the state to issue state-supported debt for capital construction projects at UMS; these amounts have ranged from a few million dollars to a recent high of \$49 million in fall 2018. For the fiscal year that will end on June 30, 2020, the system's budget for educational, general and auxiliary expenses anticipates a slightly positive bottom line consistent with the prior year's base budget. Fiscal 2021 is the great unknown, owing to the COVID-19 impact. However, the preliminary budget called for continuation of a modest 2.5% tuition increase, expected relatively flat state appropriation, careful expense adjustments in academic areas where gaps in credit hours on a year-over-year basis might suggest further belt tightening is needed resulting in an anticipated modest surplus.

Available resources

At fiscal year-end 2019, UMS had cash and investments of \$425.5 million, which we consider adequate for the rating category at 50.4% of adjusted operating expenses, and a solid 300.6% of debt outstanding. The system also had about \$209.3 million of adjusted UNA, which we also consider adequate for the rating category at 24.8% of operating expenses and 147.9% of existing debt when including the foundation's UNA. The system's largest campus, the University of Maine, located in Orono through June 30, 2019, had raised slightly in excess of \$152.2 million toward its \$200 million capital campaign goal. The campaign began on July 1, 2011, and will conclude on June 30, 2020. Also in May 2017, an \$80.6 million comprehensive campaign was approved for the University of Southern Maine.

As of fiscal year-end 2019, UMS reports its endowments' market value, combined with the endowment market values of other separately incorporated UMS affiliated fundraising organizations, was, \$424.2 million up 4.0% from the \$408.0 million at fiscal year-end 2017. Management reports that as of fiscal year-end 2019, the liquidity of the managed investment pool was quite strong, with 67.0% considered liquid on a daily and an additional 25.6% on a monthly basis. The remaining amount is either illiquid or subject to liquidation on an annual basis.

Debt and contingent liabilities

UMS' debt outstanding at fiscal 2019 year-end totaled \$141.5 million and included \$4.5 million of capital leases and \$832,000 of notes. All of the debt is fixed rate, and the system has no interest-rate swaps. We consider the maximum annual debt service debt burden low and manageable, at 2.2% of operating expenses, and good for the rating category. The current debt legislatively authorized for the system is \$350 million up from \$220 million as the system management and governance has recognized the need to reduce a critical deferred maintenance back log that at one time was estimated as high as \$720 million. The legal debt amount currently outstanding is approximately \$121 million. The system's board of trustees recently approved the issuance of revenue bonds not to exceed \$95 million for three projects at the University of Southern Maine in Portland. These projects include a 580-bed student residential facility, an approximate 425-space parking structure, and a career and student success center. The system is reviewing public private partnership options for the student residential facility and the career and student success center.

UMS pension and other postemployment benefits (OPEB) expense relative to adjusted operating expense is 5%, which we view as manageable at this time. Almost all of the current employees use a defined-contribution plan that we view as fully funded by definition; however, the university did have a defined-benefit plan that it closed to new employees in 1998. The plan is a single-employer plan that currently has a net pension liability of about \$11.5 million and was 69.7% funded as of June 30, 2019.

UMS has made some progress with its OPEB liability by instituting an OPEB trust fund (which had a market value of \$131.3 million as of June 30, 2019) to offset a \$194.6 million liability. The trust and funding arrangement eliminates the liability on UMS' balance sheet, although it does put pressure on cash flows to meet the annual required contributions, which range from \$12 million-\$20 million per year since the implementation of Governmental Accounting Standards Board Statement No. 45 in 2007.

University of Maine System--Enterprise And Financial Statistics

	--Fiscal year ended June 30--					--Medians reported for 'AA' rated public colleges and universities--
	2020	2019	2018	2017	2016	2018
Enrollment and demand						
Headcount	29,974	29,735	28,997	29,465	28,994	MNR
Full-time equivalent	21,924	22,033	21,812	21,867	21,629	35,846
Freshman acceptance rate (%)	77.8	81.6	79.8	78.3	78.9	67.8
Freshman matriculation rate (%)	20.8	22.9	21.6	22.3	24.0	MNR
Undergraduates as a % of total enrollment (%)	86.2	86.2	86.5	87.2	88.1	78.6
Freshman retention (%)	73.0	73.0	71.0	72.0	71.5	86.0
Graduation rates (six years) (%)	50.0	50.0	46.0	50.0	43.4	MNR
Income statement						
Adjusted operating revenue (\$000s)	N.A.	827,175	803,510	781,895	761,062	MNR
Adjusted operating expense (\$000s)	N.A.	844,046	805,770	770,775	759,960	MNR
Net adjusted operating income (\$000s)	N.A.	(16,871)	(2,260)	11,120	1,102	MNR
Net adjusted operating margin (%)	N.A.	(2)	(0.28)	1.44	0.15	1.50
Estimated operating gain/loss before depreciation (\$000s)	N.A.	36,123	49,450	65,180	53,519	MNR
Change in unrestricted net assets (UNA; \$000s)	N.A.	5,219	6,916	(74,950)	890	MNR
State operating appropriations (\$000s)	N.A.	211,975	210,979	212,036	201,404	MNR
State appropriations to revenue (%)	N.A.	25.6	26.3	27.1	26.5	19.2
Student dependence (%)	N.A.	47.8	47.4	46.2	45.8	39.7
Health care operations dependence (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Research dependence (%)	N.A.	16.8	17.1	17.6	17.9	MNR
Endowment and investment income dependence (%)	N.A.	1.0	0.8	0.7	0.7	1.4
Debt						
Outstanding debt (\$000s)	N.A.	141,541	150,826	162,407	154,768	828,692
Proposed debt (\$000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Total pro forma debt (\$000s)	N.A.	141,541	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	2.33	2.41	2.15	2.15	MNR
Current MADS burden (%)	N.A.	2.15	2.25	2.04	2.07	3.50
Pro forma MADS burden (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value (\$000s)	N.A.	344,740	N.A.	347,000	343,500	990,083
Related foundation market value (\$000s)	N.A.	272,936	256,212	226,999	202,691	688,435
Cash and investments (\$000s)	N.A.	425,474	407,878	391,541	367,711	MNR
UNA (\$000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR

University of Maine System--Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--					--Medians reported for 'AA' rated public colleges and universities--
	2020	2019	2018	2017	2016	2018
Adjusted UNA (\$000s)	N.A.	209,291	206,923	187,986	194,602	MNR
Cash and investments to operations (%)	N.A.	50.4	50.6	50.8	48.4	54.0
Cash and investments to debt (%)	N.A.	300.6	270.4	241.1	237.6	168.3
Cash and investments to pro forma debt (%)	N.A.	300.6	N.A.	N.A.	N.A.	MNR
Adjusted UNA to operations (%)	N.A.	24.8	25.7	24.4	25.6	35.3
Adjusted UNA plus debt service reserve to debt (%)	N.A.	147.9	137.2	115.7	125.7	97.8
Adjusted UNA plus debt service reserve to pro forma debt (%)	N.A.	147.9	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	13.8	13.3	13.0	12.2	13.0
OPEB liability to total liabilities (%)	N.A.	14.9	18.6	17.6	31.7	MNR

UNA--Unrestricted net assets. MADS--Maximum annual debt service. OPEB--Other postemployment benefits. Total adjusted operating revenue = unrestricted revenue less realized and unrealized gains/losses and financial aid. Total adjusted operating expense = unrestricted expense plus financial aid expense. Net operating margin = 100*(net adjusted operating income/adjusted operating expense). Student dependence = 100*(gross tuition revenue + auxiliary revenue) / adjusted operating revenue. Current debt service burden = 100*(current debt service expense/adjusted operating expenses). Current MADS burden = 100*(MADS expense/adjusted operating expenses). Cash and investments = cash + short-term and long-term investments. Adjusted UNA = UNA + UNA of the foundation. Average age of plant = accumulated depreciation/depreciation and amortization expense. N.A.--Not available. MNR--Median not reported.

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