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**Santa Clara Valley Transportation Authority,
California**

Credit Profile

US\$58.975 mil Sales Tax rev bnds (2000 Measure A) ser 2006 D due 04/01/2036	AA
Sale date: 08-AUG-2006	
US\$58.975 mil Sales Tax rev bnds (2000 Measure A) ser 2006 B due 04/01/2036	AA
Sale date: 08-AUG-2006	
US\$58.975 mil Sales Tax rev bnds (2000 Measure A) ser 2006 C due 04/01/2036	AA
Sale date: 08-AUG-2006	
US\$58.95 mil Sales Tax rev bnds (2000 Measure A) ser 2006 A due 04/01/2036	AA
Sale date: 08-AUG-2006	
US\$54.700 mil Sales Tax rev bnds (2000 Measure A) ser 2006 E due 04/01/2036	AA
Sale date: 08-AUG-2006	
US\$68.9 mil Sales Tax rev bnds (2000 Measure A) ser 2006 F due 04/01/2036	AA
Sale date: 08-AUG-2006	
US\$68.9 mil Sales Tax rev bnds (2000 Measure A) ser 2006 G due 04/01/2036	AA
Sale date: 08-AUG-2006	
OUTLOOK:	STABLE

Rationale

Standard & Poor's Ratings Services assigned its 'AA' rating to Santa Clara Valley Transportation Authority, Calif.'s 2006 Measure A sales tax bonds, series A-G, totaling a combined \$428.375 million.

The rating reflects:

- A broad and diverse sales tax base that encompasses San Jose and much of the Silicon Valley region and has demonstrated a long-term trend that is positive overall;
- Good annual debt service coverage based on historic and projected performance; and
- A fully funded debt service reserve.

The above strengths are somewhat offset by a relatively weak 1.3x additional bonds test (ABT). An additional weakness is the authority’s capital plan, which is likely to be financed with the issuance of parity debt, although none is anticipated before 2011.

The 2006 Measure A sales tax revenue bonds are secured by a gross pledge of a 0.5% sales tax imposed throughout Santa Clara County that was approved by voters in 2000 in association with a program of large capital projects, including the BART (Bay Area Rapid Transit) extension to San Jose. The Measure A sales tax sunsets in 2036, which is the final maturity for the 2006 bonds. Pledged revenues are collected by the state Board of Equalization and distributed directly to the bond trustee, prior to funds being released to the transportation authority for operating purposes. The authority also receives a separate source of sales tax, approved by voters in 1976, that secures \$331 million in sales tax revenue bonds under a separate indenture. The rating on the 1976 bonds was raised to ‘AA+’ due to Standard & Poor’s expectation that debt service coverage should remain much higher on the 1976 bonds than on the 2006 Measure A bonds.

The ‘AA’ rating is supported by the breadth of the authority’s service area, which encompasses most of Silicon Valley, with a total population of 1.77 million. By 2020, according to projections, the population will grow another 25%, to 2.2 million residents. The county is among the wealthiest in the state in terms of income and property, and also has one of the highest costs of living. With leading employers that include Hewlett Packard, Cisco, and Google, the job market has improved from levels reached during the recent recession, and in 2005 the unemployment rate of 5.4% was only slightly higher than the national rate of 5.2%.

Performance of pledged revenues has stabilized since 2002, when recession took hold of Silicon Valley. Beginning in 2004, sales tax revenues returned to positive territory along with regional economic improvement. Sales tax projections are based on economic analysis that factors in job growth, population trends, and earnings growth, among other data.

Santa Clara Valley Transportation Authority Sales Tax Revenues

<i>Historic</i>			<i>Projected</i>		
<i>Fiscal Year</i>	<i>Sales Tax Revenues (\$000s)</i>	<i>Change (%)</i>	<i>Fiscal Year</i>	<i>Sales Tax Revenues (\$000s)</i>	<i>Change (%)</i>
1996	122,274		2006*	152,393	5.09
1997	128,968	5.47	2007	158,020	3.69
1998	138,428	7.34	2008	164,969	4.40
1999	143,711	3.82	2009	174,393	5.71
2000	166,764	16.04	2010	184,431	5.76
2001	183,540	10.06	2011	195,126	5.80
2002	144,217	(21.42)	2012	206,523	5.84
2003	132,632	(8.03)	2013	218,672	5.88
2004	138,917	4.74			
2005	145,008	4.38			

*Estimated based on actuals for first three quarters.

The sales tax revenues collected for the authority are collected in addition to the state’s 7.25% sales tax.

Maximum annual debt service (MADS) on the Measure A 2006 bonds is \$58 million and occurs in the final four years of amortization, beginning in 2033. With lower annual debt service until 2032, the financing structure should provide a window for using surplus Measure A revenues for pay-as-you-go capital projects and

operations. Only about 18% of Measure A revenue is intended to be used for operations, but the board can budget for more than that on an annual basis.

Based on 2005 collections of sales taxes, coverage of MADS on these bonds is 2.76x. In the earlier years of the amortization, however, coverage should be much higher, or 6.7x. The 1976 bonds have MADS coverage of 8.0x based on 2005 revenues.

The authority's very substantial capital plan will require further borrowing that should constrain debt service coverage. Unlike the 1976 sales tax revenues, where surplus revenues not used for debt service fund operations, the Measure A sales tax proceeds will be largely used for capital projects. The 30-year expenditure plan calls for \$14.1 billion in projects to be financed with Measure A sales taxes, both by servicing debt used to finance projects and through pay-as-you-go capital spending. Specific capital plans through 2011 include pay-go capital spending, and no further new money bonds are planned over this five-year planning horizon. Planned pay-go capital spending of Measure A revenues provides some assurance that the authority will not bond down to its ABT, at least not in the near term. The largest of the Measure A projects will be a \$6.2 billion extension of BART to San Jose, with an expected completion date of 2016.

The 2006 Measure A bonds will be issued in seven series of auction-rate securities. Series A-D, totaling \$210.85 million, will be synthetically fixed through four LIBOR-based floating to fixed interest rate swaps with highly rated counterparties. The authority's Measure A sales tax revenue portfolio has been assigned a Standard & Poor's Debt Derivative Profile (DDP) score of '1.5' on a four-point scale, where '1' represents the lowest risk. The remaining 2006 Measure A sale tax revenue bonds, series E-G, will be unhedged, for overall variable exposure of \$192.5 million. Looking at the authority's overall debt portfolio, including the 1976 sales tax revenue bonds, overall variable-rate exposure is 39%, or \$297.225 million out of \$759.095 in overall authority sales tax revenue bonds secured by both the 1976 sales tax and the Measure A sales tax.

Outlook

The stable outlook reflects Standard & Poor's expectation both that pledged revenues will perform in a manner consistent with long-term historic performance and that the authority will not issue additional bonds more aggressively than currently anticipated by capital needs. If debt service coverage levels differ materially from those projected, the rating could be lowered.

Silicon Valley Supports Economic Base

The economic base of the authority has stabilized and retains key competitive strengths. The authority serves Santa Clara County ('AA+' issuer credit rating), which is centered in San Jose, one of California's largest cities, and other communities that form Silicon Valley. It is the fourth most populous county in California, and San Jose is the third-largest city in the state. The Silicon Valley economy is primarily located in this area, including Hewlett Packard, Intel, National Semiconductor, Lockheed Missiles and Space, IBM, and Sun Microsystems. The service area is about 45 miles south of San Francisco and 42 miles southwest of Oakland. The success of the Silicon Valley economy is attributable to several factors, including a highly educated population and the proximity of several universities, namely Stanford, San Jose State, Santa Clara University, and University of California at Berkeley (located in Alameda County). The presence of venture capital firms in Silicon Valley and in San Francisco has also supported investment in the region. Cisco Systems is the leading employer (13,000 jobs), followed by Stanford University (12,000) and Hewlett Packard (8,000). Lockheed and IBM employ 7,400

and 7,000, respectively. Google employs 3,021. The unemployment rate has steadily improved since 2002, when it was over 8%, to 5.44% in 2005.

Sales Tax Revenues A Leading Source Of Operating Funds

Operating revenues are a mix of fares and advertising revenues, grants from the state, and sales tax revenues. For operations, the authority, like other major transit providers across the U.S., relies substantially on intergovernmental support and local subsidization to meet operating budget needs. Passenger fares are only sufficient to cover a small portion of overall financial requirements. By policy, a 15% operating reserve is maintained.

The authority is a transportation district that manages and operates the bus and light rail system, including 430 diesel buses and a 42.2-mile light rail system connecting the cities of Mountain View, Sunnyvale, Santa Clara, San Jose, and Milpitas. Bus ridership in fiscal 2006 was 39.2 million, a 5.6% gain compared with 2005 and the first increase in ridership since 2001, when it reached a peak of 56.5 million.

The leading source of funds used for operating expenses is sales tax revenue from the 1976 tax, totaling \$145 million in fiscal 2005, or 62% of the budget. All but about 18.5% of Measure A sales taxes will be used to fund Measure A projects. The authority has complied with its board-approved operating reserve policy of 15% of expenditures in every year except 2002, when sales tax revenues fell 21.4%. Farebox revenues and advertising cover only a very small portion of operating expenses (about 13.7% in fiscal 2005), and remaining revenues come from state and federal transportation grants.

Management And Operations

Policies are in place that govern the authority's investment management practices, reserve levels, debt management, and use of swaps. Capital planning efforts consist of a two-stage process, with biannual updates to the short-range capital plan and updates to the long-range transit plan every three years. The authority has a biannual budget process that includes mid-year revisions according to budget performance. The authority's board is composed of 12 elected officials who are appointed by the cities they represent.

Debt

With these 2006 bonds, the authority is refunding \$371.1 million in bonds. In addition, \$45 million in new money bonds are being issued. Series A-D, totaling \$210.85 million, will be synthetically fixed through interest rate swaps. The remaining \$217.1 million will be variable.

The authority has \$328.7 million in sales tax bonds outstanding secured by the 1976 sales tax. The 1976 sales tax does not expire. With these refunding bonds, there will be \$428 million in bonds secured by the 2000 Measure A sales tax, which was approved by the required two-thirds of voters in 2000. This sales tax measure sunsets March 31, 2036.

Debt Derivative Profile

The authority has been assigned a DDP score of '1.5' for its Measure A sales tax revenue bonds. The score of '1.5', on a four-point scale where '1' is the most favorable score, indicates that the authority's swap portfolio represents very low risk.

The authority is entering into four interest rate swaps in association with its auction rate bonds, Measure A series 2006 A-D, with a combined principal amount of \$210.85 million. Each of the four swaps will be equal in size and in terms, based on amortizing notional amounts coterminous with the bonds. The long-

dated nature of the swap and a heavily back-loaded structure contribute to the score. The authority has adopted a formal swap management policy that requires highly rated counterparties, among other practices, that mitigate counterparty risk and the risk that swaps would be involuntarily terminated due to a counterparty's rating being lowered. Counterparty risk is further mitigated by the authority's practice of entering into swaps with multiple counterparties, so there is no reliance on a single counterparty. The authority has the ability to terminate the swaps at any time, at market cost.

The counterparties are Citibank, N.A. ('AA'), Banc of America Securities N.A. ('AA-'), Goldman Sachs Mitsui Marine Derivative Products L.P. ('AAA'), and Morgan Stanley Capital Services ('A+'). In return for a fixed rate of 3.8%, the authority will receive from each counterparty a floating rate equal to 65% of LIBOR. While there may be a termination payment required by the authority, this would only be required if the rating on the authority's debt was lowered to below 'BBB-', an event that is considered unlikely given its 'AA' rating.

Following the issuance of the 2006 Measure A bonds, the authority will have a considerable portion of its auction rate securities unhedged (\$297.225 million, or 39% of the \$759 million in combined outstanding principal). In order to manage variable-rate exposure and basis risk, the authority has committed to maintain reserves equal to 15% of operations, and further to set aside any net payments in the authority's favor in a "basis stabilization fund." In 2005, actual operating reserves totaled \$50 million, not including an additional \$80 million in non-operating reserves.

Legal Provisions

The ABT is a two-part test that requires 1.3x MADS coverage based on historic revenues, and 1.1x MADS coverage assuming that any unhedged variable debt is at the maximum rate (12%). A reserve fund will be funded at the lesser of MADS, 125% average annual debt service, or 10% of principal.

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