S&P Global
Ratings

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Summary:

North Hudson Sewerage Authority, New Jersey; Water/Sewer

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Credit Profile		
US$45.0 mil gross rev sr ln lse certs ser 2023 due 06/01/2044		
Long Term Rating	A+/Stable	New
North Hudson Swg Auth gross rev sr lien lse certs (AGM)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
North Hudson Swg Auth gross sr lien		
Long Term Rating	A+/Stable	Affirmed
North Hudson Swg Auth gross sr lien (BAM) (SECMKT)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'A+' long-term rating to the North Hudson Sewerage Authority (NHSA), N.J.'s series 2023 gross revenue senior-lien lease certificates.
- Additionally, S&P Global Ratings affirmed its ratings on NHSA's certificates outstanding.
- The outlook is stable.

Security

Proceeds of the certificates will be used to refinance NHSA's series 2019 certificates. As of the last audited fiscal year on Jan. 31, 2023, NHSA had $275.8 million of lease certificates and $56 million of state loans outstanding.

A gross senior-lien revenue pledge secures NHSA's certificates. The authority has agreed to make lease-rental payments to the lessor, Municipal Infrastructure Leasing 1 Inc., and we understand lease payments are not subject to appropriation risk. Under a master and head lease, NHSA contracted with this lessor, from whom the authority leases the system for 35 years in return for a lump-sum payment equal to the lease's total par amount. The LLC leases the system back to the authority for operations. NHSA makes rental payments that match certificate debt service payments, paid in equal monthly installments. During the lease term, NHSA retains all operating responsibilities.

Due to the existence of the lease, we have also considered the rating with respect to our "Issue Credit Ratings Linked to Obligors' Creditworthiness" criteria (published Nov. 20, 2019, on RatingsDirect), and we do not believe that the existence of the lease introduces any additional credit risk because there is no appropriation risk, nor is there any construction risk since the leased assets have already been constructed. Because of that, the certificate ratings match our opinion on the overall creditworthiness of NHSA.

Credit overview

Maintenance of a stable financial profile within a service territory that is immediately accessible to Manhattan and the greater New York area serves as the anchor for the rating. However, continued capital and state loan needs for its long-term control plan (LTCP) related to combined sewer overflow (CSO) mitigation and debt-to-capitalization that exceeds 70% are currently factors that limit upward potential for the rating. NHSA plans for about $106 million of capital improvements through 2028, with $62.9 million allocated to LTCP projects.

Environmental, social, and governmental

While we believe that dry weather treatment capacity is adequate to serve NHSA's customer base, it is entering into the first phase of the LTCP, which will involve additional capital spending to maintain compliance with environmental regulations. In addition, storm hardening and resiliency is an ongoing effort, but one that we believe has been implemented successfully due to a large amount of post-Sandy funding that the authority has used for reliability, redundancy, and emergency management projects.

The largest social factor that could affect NHSA's operations relates to rate affordability and allowances for late/delinquent payments. When weighting median household effective buying income (MHHEBI) by the allocated flows for each municipality served by NHSA (Hoboken, Union City, Weehawken, and West New York), the average is currently about 120% of the national average, and the monthly equivalent rates of $67.36 for 6,000 gallons of usage only is about 1.2% of MHHEBI. A future concern will be how much rates escalate to finance additional capital needs for the LTCP.

Governance risks mostly relate to management's overall financial management strategies while facing increasing capital needs, which we view as credit-supportive since management regularly updates financial projections to include these additional costs. However, pursuant to state law (N.J.S.A. 40: 14A-4.2), NHSA can only recover certain costs with a 2% annual escalator, limiting the ability to recover higher costs solely through rates. However, notable exceptions include items like capital expenses, debt service, and pension costs.

Outlook

The stable outlook reflects our view that both the financial and economic factors supporting the rating over the next several years will remain at levels consistent with historical trends, even with the additional debt plans.

Downside scenario

If NHSA's future rate increases and budgets do not support operations in a fashion consistent with or better than historical trends, the rating could be lowered. In addition, there could be downward pressure if large additional debt plans arise and financial margins deteriorate as a result.

Upside scenario

If NHSA's financial operations continue to improve over recent historical trends and we believe that the improvements are sustainable, we could raise the rating further, especially if additional longer-term debt plans become more defined. Additionally, should the authority operational procedures and policies become more in line with higher rated entities a higher rating could be possible. However, both the ongoing debt plans and unfavorable leveraged position currently serve as limitations to upward rating movement.

Credit Opinion

Financial metrics are consistent with the rating level and include debt service coverage (DSC) at the fiscal year ended Jan. 31, 2023, of about 1.5x and unrestricted cash and investments of $43.8 million representing about 662 days' cash at the end of that same period. We believe future financial performance will be consistent with historical results, based on our review of NHSA's projections made available in conjunction with the issuance of the 2023 certificates.

We believe that operational and management practices and policies are generally consistent with the rating level. Operational policies include an integrated asset management and work order system, regular communications with customers, and annual review of rates. Financial management practices include regular review of budget assumptions and performance, a capital improvement program included in the budget, a policy of maintaining unrestricted cash and investments that represent at least 180 days' operating expenses, and a 1.4x senior-lien DSC target.

We consider the certificate provisions somewhat weak, mostly reflecting our view of the additional certificates test. While additional certificates can be issued as long as projections show compliance with the rate covenant, this compliance only extends to five years after project completion. When this restriction is extended to the entirety of the debt service schedule, we view this limitation as a stronger credit feature. We would note that the rate covenant is fairly standard, and provides for a 1.15x senior-lien DSC test and a 1x total annual DSC test. In addition, a debt service reserve fund, equal to the lesser of maximum annual debt service (MADS), 10% of par, or 1.25x average annual debt service, provides additional liquidity.

NHSA is legally required to set rates to cover operating expenses and debt service. If service charges do not meet expenses, NHSA will impose annual charges on the municipalities themselves, if necessary. The authority would assess annual charges based on each municipality's latest flow. If one or more municipality does not pay, however, the remaining municipalities do not need to cover the charges; they would only be required to pay their assessed flow-based shares. The authority has never had to institute annual charges, but if this ever became necessary, the rating would likely be based on our opinion of the members' creditworthiness.

NHSA serves four municipalities immediately across the Hudson River from New York City in Hudson County:

- Union City (34% of fiscal 2023 billed wastewater flows),
- Hoboken (30%),
- West New York (27%), and
- Weehawken (9%).

A nine-member board governs the NHSA, with each municipality having two members on the board, except for Hoboken, which has three.

Since 1988, NHSA has subcontracted operations of its facilities to an operator that is part of the Jacobs Engineering Group. This long-term contract expires in 2030, and the authority treats such expenses as operating expenses. There are two wastewater treatment plants: Adams and River Road. The Adams wastewater treatment plant has a design capacity of 20.8 million gallons per day (mgd), while the River Road plant can handle 10 mgd.

NHSA directly bills its customers on a quarterly basis.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of November 9, 2023)		
North Hudson Swg Auth gross sr lien (BAM) (SECMKT)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
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Unenhanced Rating	A+(SPUR)/Stable	Affirmed
North Hudson Swg Auth grs rev sn ln lease cert		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.