

Comments on Guidelines for Interest Rate and Forward Purchase Agreements

The proposed guidelines are a major step forward in assuring better controls in the use of derivatives by our local governments.

Our comments are drawn from the experiences of Blount County with variable rate debt and swaps. These comments are directed at three major areas:

- Transparency – Assuring that key information regarding the costs and risks of these transactions is placed in the hands of the members of the legislative body and is readily available to interested members of the public.
- Conflicts of Interest – We have seen transactions where one individual, and companies he is employed by, or controls, have played the roles of bond advisor, swap advisor, underwriter, administrator/remarketing agent, and bond trustee on the same debt issuance. The conflicts in these roles are an invitation to bad practices, and should be clearly excluded by the guidelines.
- Accountability for costs – All costs of setting up and terminating derivative contracts should be clearly stated and readily available to the legislative body and interested members of the public. These costs should be clearly stated on a form similar to the CT-0253 for bond transactions.

Each of our detailed comments is referenced to a page and paragraph in the proposed Guidelines document.

- Page 2, “Debt Management Report” (1). Suggest that this report also show the average annualized interest paid on each variable rate debt obligation. In addition, also suggest that this report be required to be provided, within 30 days, to the legislative body and made part of the minutes.
- Page 3, “Derivative Management Report”. Suggest an item be added to the required contents of this report. The item should require a list of all swap agreements outstanding, where the underlying debt instruments have been refinanced, defeased, or terminated in any way. This item should include the Independent Swap Advisor’s estimate of the current costs of terminating the swaps and the cost of continuing the swaps to expiration. These swaps, left floating after the termination of the accompanying bonds, are pure speculations and need careful monitoring by the legislative body. This situation currently exists in our county. This report should also be required to be provided, within 30 days, to the legislative body and made part of its minutes.
- Page 4, first paragraph. Suggest that the Independent Swap Advisor be specifically prohibited from having any relationships to any other participant in the swap, or the underlying bond transaction.
- Page 5, second paragraph. Suggest that the review of the request be expanded to the entire Finance and Audit Committee, and that each reviewer signify their completion of the review by signing the request. Also suggest that this document be required to be provided to the legislative body at the next meeting following the completion of the review.
- Page 6, D, 4. Suggest a clarification in wording: “The governing body **shall** have an audit committee.”

- Page 8, 2. Suggest the following clarification to the wording: “This report will detail the reasons for executing the option, the details of the transaction including **all** costs related to **issuance and** exercise, and the impact on its financial position and operations.
- Page 8, 3. Suggest the following be added to Material Events. “Refunding, defeasance or termination in any way of the bonds covered by any swap.”
- Page 8, 4. The referenced report should also include the ‘mark to market’ letters on any outstanding swaps.
- Page 9, 6. The refunding, defeasance or termination of the bonds underlying any swap should be considered a termination event. This report should also be required to be provided to the legislative body at its next meeting and included in the minutes of the meeting.
- Page 10, 3, a, 1. The Independent Swap Advisor should also not have been a party to the underlying bond offering as advisor, underwriter or administrator.
- Page 10, 4, a. This is an excellent requirement for a minimum benefit for taking on the added risks of a swap. Hope you insist on this in the final guidelines.
- Page 11, 5, d. This is another excellent requirement because it prevents the costs of the swap from being buried, out of public view, in the swap contract. Hope this stays in the final version.
- Page 15, H. This report should also be required to be submitted to the legislative body and included in the minutes.