

SENATE APPROPRIATIONS COMMITTEE FISCAL NOTE

BILL NO. Senate Bill 342

PRINTER NO. 1383

AMOUNT

No Fiscal Impact

FUND

General Fund

DATE INTRODUCED

February 20, 2015

PRIME SPONSOR

Senator Folmer

DESCRIPTION AND PURPOSE OF BILL

Senate Bill 342 amends the Municipality Authorities Act and the Local Government Unit Debt Act, which are contained in Title 53 (Municipalities Generally), to put in place protections and restrictions with regard to interest rate management agreements, commonly known as "swaps" or "derivatives".

The legislation amends the Municipality Authorities Act by adding new section 5608.1, which provides that municipal authorities shall be subject to the provisions of subchapter F of chapter 82 (relating to interest rate risk and interest cost management). Chapter 82 is amended so that a local government unit may enter into interest rate management agreements (i.e. "swaps") that do not exceed 50% of the total principal amount of its outstanding debt capacity.

Senate Bill 342 further amends chapter 82 by prohibiting any payments to or on behalf of a local government unit other than periodic scheduled payments and termination payments. Effectively, this provision eliminates the use of swaps as a means of temporary cash infusion, rather than as a vehicle to reduce borrowing costs. In addition, the provision also eliminates payment of a municipality's financial advisor out of the proceeds, thereby resulting in much more independent advice and analysis.

The legislation requires that interest rate management agreements take effect within three years after the date of execution of any confirmation associated with the qualified interest rate management agreement. Presently, some swap agreements do not take effect until years into the future, thereby adding volatility and risk premised on speculation as to what rates will be at that time. Furthermore, the bill requires that any agreement ends within 10 years, unless the local government could terminate it without penalty after that time.

The legislation provides that the index or basis used for calculating the periodic scheduled payments receivable by the local government unit shall be the same index as on the associated debt.

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Senate Bill 342 amends the definition of “local government unit” in section 8002 of Title 53 so that it does not apply to cities of the first class or an authority or a municipal authority in existence on the effective date of this paragraph, formed by two or more local government units for the purpose of providing loan programs for the benefit of local government units and other authorities or municipal authorities. Further, the legislation modifies certifications required from the other party to a swap agreement as follows:

- Certifies that in executing the transactions under the qualified interest rate management agreement, the other party has complied in all material aspects with the applicable rules and regulations of the Commodity Futures Trading Commission, the Securities and Exchange Commission and the Municipal Securities Rulemaking Board to which it is subject.
- Represents and warrants that the rate or rates used to calculate amounts payable by the local government unit pursuant to the qualified interest rate management agreement is comparable to the rate or rates that it would have quoted to receive from or pay to, as applicable, a similarly situated counterparty to enter into a reasonably comparable qualified interest rate management agreement taking into full account the terms and conditions of the qualified interest rate management agreement.

Senate Bill 342 requires local governments to report quarterly on the performance of the qualified interest rate management agreement at a public meeting. The bill also requires the other party to the agreement to make certifications to the local government that it has disclosed relevant information and has acted in good faith.

The act shall take effect in 60 days.

FISCAL IMPACT:

Senate Bill 342 will have no adverse fiscal impact on Commonwealth or local funds.

Because the legislation places protections and restrictions on the use of swaps, Senate Bill 342 may further protect communities against transactions that threaten their fiscal well-being.