
Financial Services Reform and its Impact on the Municipal Market

“Secondary Effect - Swaps”

CDIAC Workshop

October 6, 2010

2010 – Dodd/Frank Act and GASB 53

* Dodd/Frank Act

- Who will it affect?
- Will it affect existing transactions?
- How will it affect future transactions?
- When does it take effect?

* GASB 53

- When will it be implemented?
- Who will it effect?
- How do I complete the analysis?
- What impact will it have on my balance sheet and income statement?

Dodd/Frank: Exchange Requirement

- * None, if the muni is an “eligible contract participant”:
 - * the muni has \$50 million in discretionary assets; OR
 - * the counterparty is a bank (or guaranteed by a bank)

Dodd/Frank: Clearance Requirement

- * None, if an “end user exemption” is claimed:
 - * one of the counterparties is not a financial entity;
 - * using swaps to hedge a “commercial risk”; AND
 - * issuer notifies the SEC or CFTC how it meets its financial obligations

Dodd/Frank - Capital and Margin Requirements

- * Margin Requirement – none for municipal counterparties, unless:
 - the municipal counterparty qualifies as a swap dealer
 - the municipal counterparty qualifies as a major swap participant
- * Impact on dealers could significantly increase execution costs
- * Collateral requirements are not intended to impact “end users”

Dodd/Frank: Fiduciary Responsibilities

- * Swap Dealers, unless.....the issuer uses a Financial Advisor.
- * Swaps regulated by CFTC and SEC (Advisors by MSRB)

Dodd/Frank - Municipal Disclosure

- * GAO to study “enhanced disclosure” in the Municipal Markets
- * GOA to study the Municipal Securities market
 - an analysis of the mechanisms for trading, quality of trade execution, market transparency, trade reporting, price discovery, settlement, clearing, and credit enhancements
 - provide recommendations on how to improve transparency, fairness and liquidity
 - potential uses of derivatives

ALERT: Floating Rate Debt Disclosure

- * Types of Variable Rate Debt
 - Auction Rate Securities
 - Status
 - Variable Rate Demand Notes
 - LOC providers w/ratings
 - LOC rollover dates
 - Notes subject to “self liquidity”
 - Other types of variable rate exposure
 - Indexed Notes
 - “Direct Purchase” Notes w/terms
 - Synthetic Floating
 - other

GASB 53 - What You Should Know

- Begins FY2010
- The “Fair Value” of Derivatives is to be Reported in the Financial Statements
- If the Derivative is a “Hedge”
 - Annual Changes in Fair Value are Deferred
- If the Derivative is not a “Hedge”
 - Annual Changes in Fair Value Represented as a Gain or Loss

GASB 53 -Evaluating Effectiveness

- Consistent Critical Terms
- Quantitative Methods
 - Synthetic Instrument Method
 - Dollar-Offset Method
 - Regression Analysis
 - Other?