

Corporate Bonds

FOR CONSIDERATION

September 29, 2005

TO: The Directors

FROM: Charles A. Gargano

SUBJECT: Interest Rate Exchange or Similar Agreements

REQUEST FOR: Authorization to Adopt Guidelines for Use of Interest Rate Exchange or Similar Agreements and Delegate Authority to Bond Financing Committee

I. INTRODUCTION/BACKGROUND

Certain Bonds issued by the Corporation may be subject to interest rate exchange or similar agreements ("Swaps") which may be utilized to hedge the Corporation's risks.

In order to provide a uniform procedure for evaluation and entering into Swaps, staff of the Corporation proposes that the Corporation adopt guidelines for the use of Swaps (the "Guidelines") which govern the procurement, terms, reporting and collateralization of such agreements. A copy of such Guidelines is attached. The Bond Financing Committee, on behalf of the Corporation, has previously adopted similar guidelines for use in bond issuances supported by State appropriations.

II. REQUESTED ACTION

At this time you are being requested to approve the adoption of the attached Guidelines and confirm the Bond Financing Committee authorization to approve the terms and conditions of interest rate exchange agreements.

Attachments

Resolution
Guidelines

September 29, 2005

NEW YORK STATE URBAN DEVELOPMENT CORPORATION
RESOLUTION ADOPTING GUIDELINES FOR USE OF CORPORATE SWAPS

WHEREAS, the New York State Urban Development Corporation (the "Corporation") deems it advisable to provide for the possible use of interest rate exchange agreements or similar agreements ("Swaps") in connection with bonds issued or to be issued under its Corporate Purpose Bonds General Resolution, or other bonds not supported by State appropriations, by adopting guidelines setting forth policies and procedures for the evaluation, usage, awarding, monitoring and reporting of these Swaps and the counterparties thereto; and

WHEREAS, the guidelines provide, among other things, that the Corporation may select counterparties either through a competitive bidding process or through negotiation with one or more individual counterparties;

NOW THEREFORE, based on the materials submitted herewith, the Corporation hereby adopts the following:

RESOLVED, the Guidelines for Use of Corporate Swaps presented to the Directors herewith are hereby approved and adopted.

RESOLVED, the Bond Financing Committee is authorized to take any and all actions with respect to evaluating and entering into Swaps.

RESOLVED, that all actions heretofore taken in regard to the adoption of guidelines for use of interest rate exchange or similar agreements by authorized officers and staff of the Corporation, are hereby ratified, confirmed and approved.

 Empire State Development Corporation

**NEW YORK STATE
URBAN DEVELOPMENT CORPORATION**

GUIDELINES FOR THE USE OF CORPORATE SWAPS

1. **Conditions under which Contracts can be Entered Into.**

The conditions under which the Corporation and any subsidiary may enter into one or more interest rate exchange agreements (“Corporate Swaps”) that are not subject to the provisions of Article 5-D of the State Finance Law are fivefold:

- The swap transaction must meet the terms of these Guidelines;
- The Corporation shall have received the legal opinion of a nationally recognized bond counsel firm (which opinion may be a reasoned opinion) that the Corporate Swap is a legal, valid and binding obligation of the Corporation;
- The Bond Financing Committee shall have adopted a resolution authorizing the execution and delivery of the Corporate Swap; and selected a counterparty in conformity with these guidelines.
- The term of any Corporate Swap shall not exceed the final maturity of the bonds, notes or other obligations of the Corporation issued or outstanding in connection with such agreement.
- The Corporation has retained an approved swap advisor, and the swap advisor concurs with the transaction and has provided any necessary opinion including a fair market opinion with respect to prevailing interest rates.

2. **Purpose of Corporate Swap.**

The Corporation may enter into one or more interest rate exchange or similar agreements if each such agreement is reasonably expected to —

- reduce or hedge an exposure to changes in interest rates; or
- result in a lower net cost of borrowing with respect to the related debt obligations; or

- provide benefits and/or flexibility to the Corporation with respect to financial exposure or financial position.

The Corporation shall not enter into any Corporate Swap for the purpose of speculation.

3. **Methods for Contract Solicitation and Procurement.**

The Corporation may procure Corporate Swaps either through a competitive bidding process or through negotiation with one or more counterparties—

- **Competitive** – The minimum number of counterparties solicited and bidding shall be three. The Corporation may allow one or more counterparties to match the winning bid up to a predetermined level of notional amount. Bids shall be solicited through bid proposal prepared by the Corporation or by the Corporation’s swap advisor.
- **Negotiated** – The Corporation’s swap advisor shall determine the mid-market swap rate on the day of the swap trade and shall negotiate dealer profit with counterparties designated by resolution of the Bond Financing Committee.

The Corporation’s swap advisor shall render its written opinion as of the trade date that the terms and conditions of any Corporate Swap procured on a negotiated basis reflect the fair market value of the swap as of the trade date.

4. **Form and Content of Contracts.**

The form and content of the Corporate Swaps will be governed by—

- ISDA Master Agreement, the standard swap document negotiated between the Corporation and each counterparty;
- ISDA Schedule, which details the general provisions of the swaps between the Corporation and a particular counterparty; and
- ISDA Confirm, which will detail the actual swap trade, akin to the buy-and-sell confirm of a stock trade made by an individual investor.

The Bond Financing Committee will approve the form of each ISDA Agreement and Schedule. Each individual swap confirm will be approved by a designated officer of the Corporation subject to parameters approved by the Bond Financing Committee.

5. **Certain Risk Exposure Limitations.**

The Corporation shall not enter into a Corporate Swap that will result in the Corporation having credit exposure to a single counterparty on Corporate Swaps exceeding the larger of (i) 50% of the total counterparty exposure on Corporate Swaps or (ii) \$250 million in notional amount.

6. *Standards for Counterparty Selection.*

The standards for selection of counterparties for negotiated transactions as well as for solicitation of candidates for solicitation of competitive bids are multiple:

- Each counterparty shall have a long-term credit rating from at least one nationally recognized rating agency that is within its two highest investment grade categories and a long-term credit rating from any other rating agency that is within its three highest investment grade categories or the payment obligations of the counterparty shall be unconditionally guaranteed by an entity with such credit ratings.
- Each counterparty should have recent substantial and significant experience in the derivatives market.
- Each counterparty should currently have a substantial and significant position in the municipal bond market.
- Each counterparty should currently run a two-way derivatives book that facilitates hedging.
- Each counterparty should currently demonstrate the capability to develop creative and innovative ideas,
- The relationship with and understanding of the needs of the Corporation and the State shall be considered; and
- The Corporation shall consider any other factors deemed appropriate.

7. *Procurement of Enhancement.*

Credit enhancement may be procured for the underlying bonds and for the interest rate exchange agreement from nationally recognized providers of such products. A credit enhancement will be utilized only if it enhances the overall economics of the transaction for the Corporation.

8. *Collateralization for Securing Financial Interests in Contracts.*

The Corporation will require collateralization if the counterparty's long-term credit rating from a nationally recognized rating agency falls below required ratings stated in the agreement. The Corporation will consider bilateral and symmetrical collateral-posting provisions when swap insurance is not obtained and such provisions are in the best interest of the Corporation. Such collateral shall consist of direct obligations of, or obligations the principal and interest on which are guaranteed by, the United States of America (including cash) with a net market value of at least one hundred two percent of the net market value of the contract to the Authority ("collateral

requirement"). Any collateral agreement shall require that the net market value of the contract and the collateral be marked-to-market periodically, but not less than once each month. If the market value of the collateral shall be found to be less than one hundred two percent of the net market value of the contract to the Authority, than the counterparty shall be required to post additional collateral to meet such requirement.

9. *Consideration of Long-Term Implications.*

The Bond Financing Committee is authorized to approve swaps on behalf of the Corporation, however, the Bond Financing Committee shall not authorize any Corporate Swap without understanding and evaluating all associated risks and determining that the benefits of such agreement more than offset any risks incurred under such agreement. As part of the process of Bond Financing Committee approval for each swap transaction, Corporation staff shall present to the Bond Financing Committee an overall plan of finance incorporating the proposed swap transaction that evaluates and quantifies, to the greatest extent possible, the risks and benefits of entering into the Corporate Swap within the contexts of the related bond financing and the Corporations total outstanding Corporate Bond indebtedness.

The Corporation shall also consider the long-term implications associated with entering into such agreements, including the following:

- costs of borrowing;
- historical trends;
- use of capacity for variable-rate bonds and related credit enhancements; and
- any potential impact on the future ability to call bonds, including opportunities to refund related debt obligations.

Under a Corporate Swap, the Corporation may be either the floating-rate or fixed-rate payor. The Corporation may also provide for the establishment of maximum or minimum interest rates (or both), payable thereunder and for any other protections designed to limit exposure to changes in interest rates.

The Bond Financing Committee shall periodically evaluate swap agreements entered into by the Corporation for risks and exposures including, but not limited to, the following categories:

- counterparty risk;
- termination risk;
- rollover risk;
- basis risk;
- tax event risk; and
- amortization risk.

10. *Reflection of Contracts in Financial Statements.*

Pursuant to GASB, the Corporate Swaps will be reflected in the Corporation's annual financial statements.

11. *Financial Monitoring.*

Staff will prepare and deliver reports on a quarterly basis to the Bond Financing Committee including the following information covering each of the Corporate Swaps approved pursuant to these Guidelines:

- a description of the contract, including a summary of its terms and conditions (such as notional amounts, rates, terms, bases or indices employed) and a description of the counterparty and its credit ratings;
- the value of the Bond Market Association (BMA) index and/or such other indices applicable to such agreement;
- any amounts which were required to be paid and received, and any amounts which actually were paid and received, under such agreement since execution or the previous such report (whichever is later);
- the status of any credit enhancement, liquidity facility or reserves associated with the agreement, including an accounting of all costs and expenses incurred (whether or not incurred in conjunction with the procurement of such credit enhancement or liquidity facilities); and
- the mark-to-market valuation of such agreement, and an assessment of counterparty risk, termination risk, and other associated risks, and the amount of collateral that has been required to be posted, if any, and the amount that has been actually posted.