Approved _____ Mayor
Veto _____
Override _____

Agenda Item No. 8(E)(1)(C)
06-05-07

OFFICIAL FILE COPY
CLERK OF THE BOARD
OF COUNTY COMMISSIONERS
MIAMI-DADE COUNTY, FLORIDA

RESOLUTION NO. R-664-07

RESOLUTION APPROVING MODIFICATION TO INTEREST RATE SWAP WITH RICE FINANCIAL PRODUCTS COMPANY RELATED TO THE COUNTY'S WATER AND SEWER BONDS SERIES 1994 AND SERIES 1999 WHICH WILL PROVIDE ECONOMIC BENEFIT TO MIAMI-DADE COUNTY AS RECOMMENDED BY THE COUNTY'S SWAP FINANCIAL ADVISOR; AND DELEGATING TO FINANCE DIRECTOR THE AUTHORITY TO FINALIZE AND EXECUTE MODIFICATION

WHEREAS, this Board wishes to approve the modification of an interest rate swap with Rice Financial Products Company (the "Swap") that is related to the County's Water and Sewer Bonds, Series 1994 and Series 1999, respectively, (collectively, the "Bonds") in the manner described in the accompanying County Manager's memorandum ("Memorandum") which is incorporated in this resolution by reference and as recommended by Swap Financial Group, LLC., the County's swap financial advisor (the "Swap Financial Advisor"); and

WHEREAS, this Board wishes to delegate to the Finance Director the authority to finalize and execute the Swap modification within the parameters described in the Memorandum,

NOW, THEREFORE, BE IT RESOLVED BY THE BOARD OF COUNTY COMMISSIONERS OF MIAMI-DADE COUNTY, FLORIDA, that:

Section 1. The Board approves the modification to the Swap in the manner described in the Memorandum.

Section 2. The Board delegates to the Finance Director the authority to finalize the modification of the Swap in accordance with the terms described in the Memorandum after

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consultation with the Director of the Miami-Dade Water and Sewer Department, the Office of the Miami-Dade County Attorney and the Swap Financial Advisor; and to execute such documents that are necessary to effectuate the modification of the Swap, after consultation with the Office of the Miami-Dade County Attorney. The execution of any such documents by the Finance Director shall be conclusive evidence of the Board's approval of such documents.

If the Series 1994 and Series 1999 Bonds or any other series of Bonds to which the Swap is associated is refunded, called, or tendered, the Board further authorizes the Finance Director to associate the Swap to any other series of Bonds after consultation with the Office of the Miami-Dade County Attorney and the Swap Financial Advisor.

Section 3. The Finance Director, the Clerk of the Board, the Office of the Miami-Dade County Attorney, and other officers, employees and agents of the County are authorized and directed to do all acts and things and to execute and deliver any and all documents and certificates which they deem necessary or advisable in order to effectuate the modification of the Swap. In the event that the Finance Director or the Clerk of the Board is unable to execute and deliver the modification of Swap, such documents shall be executed and delivered by the respective designee of such officer or official or any other duly authorized officer or official of the County.

Section 4. The provisions of Resolution No. R-1198-05, as amended, requiring that any contracts of the County with third parties be executed and finalized prior to their placement on the committee agenda is waived at the request of the County Manager for the reasons set forth in the Memorandum.

The foregoing resolution was offered by Commissioner Dennis C. Moss, who moved its adoption. The motion was seconded by Commissioner Dorrin D. Rolle and upon being put to a vote, the vote was as follows:

Bruno A. Barreiro, Chairman	aye		
Barbara J. Jordan, Vice-Chairwoman	aye		
Jose "Pepe" Diaz	absent	Audrey M. Edmonson	aye
Carlos A. Gimenez	aye	Sally A. Heyman	aye
Joe A. Martinez	aye	Dennis C. Moss	aye
Dorrin D. Rolle	aye	Natacha Seijas	absent
Katy Sorenson	absent	Rebeca Sosa	aye
Sen. Javier D. Souto	absent		

The Chairperson thereupon declared the resolution duly passed and adopted this 5th day of June, 2007. This resolution shall become effective ten (10) days after the date of its adoption unless vetoed by the Mayor, and if vetoed, shall become effective only upon an override by this Board.

MIAMI-DADE COUNTY, FLORIDA
BY ITS BOARD OF COUNTY
COMMISSIONERS

HARVEY RUVIN, CLERK

COUNTY COMMISSIONERS DADE COUNTY FLORIDA

KAY SULLIVAN
Deputy Clerk

Approved by County Attorney as
to form and legal sufficiency

Gerald T. Heffernan

Swap Financial Group

Swap Financial Group, LLC
76 South Orange Avenue, Suite 6
South Orange, NJ 07079
(973) 378-5500, fax (973) 378-5575

MEMORANDUM

To:	Rachel Baum Miami-Dade County
From:	Peter Shapiro Swap Financial Group
Concerning:	CMS swap for Water & Sewer with Rice Financial Products
Date:	April 8, 2007

At your request, we have reviewed the proposal made by Rice Financial Products ("Rice") to amend its existing swap ("the Existing Swap") with the County's Water and Sewer System. The proposed amendment ("the Amended Swap") would change the floating rate formula on the Existing Swap from one based on one-month LIBOR to one based on the 10-year LIBOR Constant Maturity Swap (referred to as either "10-year LIBOR" or "10-year LIBOR CMS"). Based on our review of the proposed transaction, we recommend that the County enter into it as a form of diversification and a potential enhancement to the financial benefit of the Existing Swap.

While the County has received many proposals for CMS swaps, Rice has included in their proposal a unique aspect that would reduce the County's risk of negative cash flow in the near term. Rice has agreed to incorporate a provision (known as a "collar") that would eliminate the risk that the new floating rate the County would receive would be less than the existing floating rate for a period of two years. As outlined below, we believe this aspect of their proposal has particular merit.

CMS swaps have been widely marketed over the past two years as a means to profit from expected future steepening of the yield curve. Today's yield curve – which is the graphical depiction of interest rates at various maturities, extending from the shortest to the longest – is unusually flat, with short-term rates equal to or higher than long-term rates. The current condition is inconsistent with most other historical periods, and should logically not persist, as investors normally demand higher yields for tying up their money for longer periods of time. Today's anomaly results from conflicting tendencies on the two ends of the curve: The short end, which is primarily driven by the Federal Reserve System's policymaking, has moved upward sharply. The Fed Funds rate was 1.00% in mid-2004; it is 5.25% today, reflective of the Fed's concern with inflation. The long end, which is market driven, reflects traders' and investors' beliefs that the sharp increase in Fed Funds, and the accompanying decline in the housing market, will result in an economic slowdown. If the slowdown emerges, the Fed will likely cut short-term

Memorandum

MIAMI-DADE COUNTY

Date: June 5, 2007

Agenda Item No. 8(E)(1)(C)

To: Honorable Chairman Bruno A. Barreiro
and Members, Board of County Commissioners

From: George M. Burgess
County Manager

Subject: Resolution Authorizing a Modification to a Swap with Rice Financial Products Company For the Water and Sewer System

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Recommendation

It is recommended that the Board of County Commissioners adopt the accompanying resolution ("Swap Resolution") approving a modification of the basis swap with Rice Financial Products Company ("Rice"), associated with certain Water & Sewer System Revenue Bonds, which will provide an anticipated economic benefit to the County as recommended by the County's swap advisor. The Swap Resolution sets forth the terms and conditions to be satisfied prior to closing on the swap transaction after consultation with the swap advisor and the rating agencies.

Scope

The impact of this transaction is countywide.

Fiscal Impact/Funding Source

It is expected this transaction will have a positive impact on the Water and Sewer Department budget. It is projected that this modification to the Swap would generate approximately $1.7 million annually in additional debt service savings for a present value over the life of the transaction of $22.5 million. Actual additional savings will not be determined until they occur. While it is unlikely that the Swap will not generate savings, should this occur, the Swap payments will be paid with Water and Sewer Department revenues.

Track Record/Monitor

The County has entered into nine (9) swaps. Two (2) of these are Water and Sewer Department related swaps, with Rice Financial Products Company commencing in 1994. Rice is a national, active trader in swaps. Rice's Guarantor has an Aaa/AA- rating. The Water and Sewer Department and the Finance Department, with input from the County's swap advisor have been monitoring the Swap and will continue to do so if the proposed modifications are approved.

Background

On March 6, 2006 the County entered into a $205.07 million notional amount, basis swap with RFPC, Ltd., a division of Rice, as counterparty, in regards to the Water & Sewer Revenue Bonds, Series 1994 and Series 1999A. The guarantor for the counterparty is the Bank of New York, a counterparty rated Aaa by Moody's and AA- by S&P. The swap transaction is based on the County paying the Bond Market Association Municipal Swap Index ("BMA"), an index of tax exempt rates, divided by a factor of 0.604 and Rice paying the average three month London InterBank Offer Rate ("3M LIBOR"), an index of taxable rates, plus a constant to the County. The constant was negotiated at time of pricing to be 1.58%. The termination date of the swap is October 1, 2029.

Rice has submitted a proposal (the "Proposal") to modify the above Swap by substituting the 3M LIBOR plus a constant of 1.58% with an average ten year London InterBank Offer Rate ("10Y

LIBOR") plus a new constant of 1.58%and implement a collar, as defined below, for a period not to exceed the first two years of the modification. The Proposal states that this modification is expected to generate approximately $1.7 million annually in additional debt service savings for a present value over the life of the transaction of $22.5 million. Swap Financial Group, LLC, the County's swap financial advisor ("Swap Advisor"), reviewed the Proposal and at the County's request evaluated the Water and Sewer Department's ("Department") exposure related to (i) interest rate changes, (ii) tax law changes; (iii) counterparty risks; and (iv) the Department's outstanding volume of swaps. Attached to this memorandum is the recommendation from the Swap Advisor.

Upon further discussion with Rice and the Swap Advisor, and based on the Department's current level of swap exposure and the County's risk tolerance, it is recommended by the Swap Advisor that the County modify the basis swap with Rice by substituting a percentage of 10Y LIBOR plus a constant of 1.58%. The percentage of the 10Y LIBOR will be determined at the time of pricing. The higher the percentage the greater opportunity for enhanced savings as the yield curve (representing the difference between short-term and long-term rates) slopes upward. Because the current yield curve is relatively flat, the Proposal includes a provision (known as a "collar") that would eliminate the risk that the benefit the County would receive would be less than the existing swap, while allowing the County to receive partial benefit of the modification for a period not to exceed the two years. The collar minimizes (not less than zero) and maximizes (not greater than .25%) the amount of benefit the modification would generate during the collar period.

Based on the historical relationship between 3M LIBOR and 10Y LIBOR, it is expected that this modification to the Swap would generate approximately $1.7 million annually in additional debt service savings for a present value over the life of the transaction of $22.5 million. Actual savings will not be determined until they occur.

The primary risk associated with the existing swap is the relationship between tax-exempt interest rates and taxable interest rates, specifically changes in the ratio between two interest rates. If federal income tax rates are significantly reduced during the term of the transaction, BMA (the tax exempt interest rate) would rise to levels that trade closer to LIBOR (the taxable interest rate), and thus reduce the benefit being received or increase the probability of payments by the County to Rice. The tax event risk becomes a potential liability to the County when the BMA/LIBOR ratio has narrowed to a point that it offsets the constant. Risk associated with the modification to the swap is that the current flat yield curve will not return to historical levels and will be inverted or remain flat after the collar period. Such inversion or flatness will cause the County to receive a lower benefit than that of the current structure. If the yield curve is slightly to normally upward sloping, the County should recognize the anticipated additional benefit. If it is steeply upward sloping, the County will benefit more than anticipated.

The following conditions are recommended:

- The notional amount of the swap will remain at $205.07 million provided that entering into this modification to the swap will not cause the rating agencies to lower the underlying, uninsured rating on the Water and Sewer System Revenue Bonds.

- For a period not to exceed the first two years, the County shall enter into a collar whereby, the County shall pay BMA divided by 0.604 and Rice shall pay 1.58% plus:

- 3M LIBOR **if** 10Y LIBOR is less than 3M LIBOR;

- 10Y LIBOR **if** 10Y LIBOR is less than 3M LIBOR plus the Ceiling Level (The Ceiling Level will be equal to an amount in basis points, no less than 25 basis points, to be determined at pricing of the collar.); and

- 3M LIBOR plus the Ceiling Level **if** 10Y LIBOR is greater than 3M LIBOR plus the Ceiling Level.

- After the collar period, the County will pay BMA divided by 0.604 and receive a percentage of 10Y LIBOR plus 1.58%. The percentage shall not be lower than 85% and shall be determined at pricing.

- The term of the swap will be October 1, 2029.

- The long term credit ratings of the Counterparty's Credit Support Provider, the Bank of New York as guarantor of Rice's obligation under the transaction ("Guarantor"), will be rated in the double 'A' category or better from at least one of the three nationally recognized rating agencies at the time of closing as specified in the County's Master Swap Policy and the transaction shall be subject to collateralization if there is a credit downgrade the Guarantor throughout the term of the Transaction below the double 'A' rating category as specified in the County's Master Swap Policy.

- The Swap Advisor will issue a written confirmation that the County received a fair pricing for the transaction.

Resolution No. R-1198-05 provides that any County contracts with third parties be finalized prior to their placement on the committee agenda. The execution of the swap cannot occur until after the attached Swap Resolution authorizing the swap is effective. Inasmuch as an authorization to enter into the Swap is necessary prior the execution of the Swap, the final details cannot be concluded at the time the Swap Resolution is adopted. Therefore, a waiver of the requirements of Resolution No. R-1198-05 is necessary. A copy of the confirmation in substantial form with blanks to be determined at pricing with the modifications to the current swap agreement is attached.

Assistant County Manager

MEMORANDUM

(Revised)

TO: Honorable Chairman Bruno A. Barreiro and Members, Board of County Commissioners

DATE: June 5, 2007

FROM: Murray A. Greenberg County Attorney

SUBJECT: Agenda Item No. 8(E)(1)(C)

Please note any items checked.

_____ **"4-Day Rule" ("3-Day Rule" for committees) applicable if raised**

_____ **6 weeks required between first reading and public hearing**

_____ **4 weeks notification to municipal officials required prior to public hearing**

_____ **Decreases revenues or increases expenditures without balancing budget**

_____ **Budget required**

_____ **Statement of fiscal impact required**

_____ **Bid waiver requiring County Manager's written recommendation**

_____ **Ordinance creating a new board requires detailed County Manager's report for public hearing**

_____ **Housekeeping item (no policy decision required)**

_____ **No committee review**

rates, restoring an upward slope to the yield curve. If the economy continues to be strong, however, long-term rates will likely rise, also restoring the upward slope. It is possible, however, that a conflicted picture will continue, prolonging the flatness of the curve.

The Amended Swap would allow Miami-Dade County to benefit from a future increase in yield curve steepness by receiving a rate based on 10-year LIBOR rather than one-month LIBOR. Now is the best time to enter into the Amended Swap, as the current flatness of the yield curve makes the cost of the transaction cheaper. The two floating rates do not trade even with one another, even in today's flat curve environment. Rice has estimated that the one-month LIBOR rate could be replaced with the 10-year LIBOR rate at the cost of a reduction in the annual constant that is included in the formula on the Existing Swap. (Actual pricing will depend on market conditions at the time the swap is entered into.) Instead of reducing the constant, the County could receive a somewhat reduced percentage of 10-year LIBOR.

In either case, under current market conditions, the County would suffer a loss of cash flow if the Amended Swap commenced today, because the yield curve is flat to inverted. Two mechanisms have been proposed to obviate this problem: (1) setting the effective date of the Amended Swap a year or more in the future; or (2) following Rice's innovative proposal, restricting the positive or negative return on the Amended Swap to a band, known as a "collar", such that the worst the Amended Swap can do is break event and the best it can do is produce a small financial improvement for the County.. The collar would apply for only the first two years of the swap, after which, presumably, the yield curve would have a great chance to resume its historically normal upward slope. We believe the collar mechanism suggested by Rice has merit.

One open element in the structure of the transaction is whether the new 10-year floating rate should be based on 10-year LIBOR minus a fixed spread measured in basis points (which is effectively what Rice has proposed when they suggest lowering the constant on the Existing Swap) or on a percentage of 10-year LIBOR that would be somewhat lower than 100%. We have analyzed the historical data, and it shows that the lower-constant version performs better than the lower-percentage formula when 10-year LIBOR is lower than 5.67%. When it is above 5.67%, the lower-percentage formula performs better. In trying to determine which outcome would be best for Miami-Dade County and the Water and Sewer Syste, we can look it the question in two ways: (1) Looking forward, is 10-year LIBOR likely to be higher or lower than 5.67% over the 22 ½ years remaining on the Existing Swap? Or, (2) Which rate environment – above 5.67% or below 5.67% – is likely to be more generally stressful for the County financially, making it so that it would be best to have this transaction produce its strongest results in that environment? Our recommendation is to use the lower-percentage formula, based on the facts that (1) no one knows what future rates will be, and (2) the County and the Water and Sewer System will probably be more in need of added financial resources in a higher interest rate environment than in a lower one. In any case, our analysis shows that the net difference in the two structures is relatively small.

In conclusion, we recommend that the Amended Swap move forward, including the collar structure that Rice has proposed. Either a lower-percentage structure or a lower-constant structure is workable; we favor the lower-percentage structure. Upon approval, we will work with the County's finance team to make sure pricing is satisfactory.