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Pennsylvania Proposes Restrictions on Municipal Interest Rate Swaps

HIGHLIGHTS:

- New legislation has been proposed in Pennsylvania imposing specific restrictions and parameters on interest rate swaps entered into by certain cities, counties and municipal authorities in the Commonwealth, and imposing new obligations on the providers of such interest rate swaps.
- The First Class City and County Interest Rate Management Agreement Act (H.B. 884) has been referred to the House Committee on Local Government for further consideration. It is anticipated that a similar bill will be introduced in the state Senate shortly.

New legislation has been proposed in Pennsylvania imposing specific restrictions and parameters on interest rate swaps entered into by certain cities, counties and municipal authorities in the Commonwealth, and imposing new obligations on the providers of such interest rate swaps. The bill (H.B. 884) – First Class City and County Interest Rate Management Agreement Act – was introduced in the House of Representatives on March 19, 2019. The bill restates certain restrictions first proposed earlier this year in H.B. 320 and S.B. 206, introduced as part of a series of legislation in both houses of the General Assembly intended to address municipal government reform.

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Which Municipal Entities Are Covered (Each a “Contracting Authority”)

- Cities of the first class (those having a population of at least 1 million inhabitants)
- Counties of the first class (those having a population of at least 1.5 million inhabitants)
- Certain municipal authorities

Which Agreements Are Covered

- Any agreement which “in the judgment of the contracting authority is designed to manage interest rate risk or interest cost of the contracting authority on any debt or other debt-related obligations a contracting authority is authorized to incur,” and expressly references swaps, interest rate caps, collars, corridors, ceiling and floor agreements, forward agreements, float agreements and other similar arrangements.

Restrictions and Parameters

- Each interest rate management agreement or related confirmation must be **authorized and awarded by resolution** of the contracting authority
- No payments may be made to or on behalf of a contracting authority by the other party except **periodic scheduled payments, termination payments and attorney fees and other consultant fees** incurred in connection with entering into an interest rate management agreement

- Periodic scheduled payments must commence **not later than three years** after the date of the related confirmation
- The index or basis used to calculate the periodic scheduled payments to be received by the contracting authority must be “**substantially similar**” to the index or basis used to calculate the interest due on the associated debt
- At the time of execution, the notional amount of each interest rate management agreement, together with the notional amount of outstanding interest rate management agreements, **cannot exceed 30 percent of the total principal amount** of the debt sharing the same source of payment as such interest rate management agreements
- Payments received by the contracting authority **must be deposited in a payment account** and used for certain enumerated purposes
- The scheduled expiration date of an interest rate management agreement **cannot exceed 10 years** from the date of the related confirmation unless the interest rate management agreement allows the contracting authority to **terminate at any time after 10 years without making a termination payment**

Provider Obligations

Each provider of an interest rate management agreement **must acknowledge the following in a certification:**

- that the contracting authority is a political subdivision or municipal authority
- that the provider has read the law
- that the contracting authority may only enter into an interest rate management agreement to manage interest rate risk or interest cost on debt or other debt-related obligations of the contracting authority
- that it will notify the state’s Department of Community and Economic Development, in writing, promptly upon payment of a termination payment by the contracting authority, including the date and amount of the payment and identity of the interest rate management agreement under which it was made

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