

**RESOLUTION NO. 13-13810**

**A RESOLUTION UPDATING THE DISTRICT'S  
INTEREST RATE HEDGE POLICY**

**FACTUAL BACKGROUND AND REASONS FOR ACTION**

The District has, and will, issue debt obligations as necessary to maintain good and efficient operations of District facilities. In managing District debt, staff is proactive in utilizing financing alternatives, such as refinancing and structuring, as authorized under District bond resolutions to reduce the costs of borrowing. As a means of further reducing borrowing costs, staff investigates and employs other financing alternatives including interest rate agreements (also known as swaps, hedges, or payment agreements) as an integral part of the District's bond risk management program. Such agreements are specifically authorized by RCW 39.96.

The initial interest rate swap policy was adopted in 2005 and amended from time to time to conform to changing business conditions. Pursuant to Resolution No. 11-13629, adopted by the District's Board of Commissioners (the "Commission") on February 22, 2011, the District adopted the current Interest Rate Hedge Policy to establish the manner of execution of hedges, to provide for security and payment provisions, risk considerations and certain other relevant provisions and to provide guidelines for the use and management of all interest rate management agreements. This Policy supports the District's Strategic Plan by developing and implementing policies to assure financial stability for the long term.

The current Interest Rate Hedge Policy requires that, in addition to making regular presentations and semi-annual swap reports to the Commission, the Chief Financial Officer and District staff will review the Interest Rate Hedge Policy annually and recommend any updates or changes to the Interest Rate Hedge Policy for review by the Commission.

District staff has reviewed the Interest Rate Hedge Policy and recommends that the Interest Rate Hedge Policy be amended and restated in substantially the form of the Amended and Restated Interest Rate Hedge Policy attached hereto as Exhibit A. The proposed changes are designed to conform the Policy with requirements of and market practices resulting from the Wall Street Transparency and Accountability Act of 2010, as supplemented and amended (including related regulations, commonly referred to as "Dodd-Frank").

In connection with the implementation of Dodd-Frank, the District must: (i) obtain a "legal entity identifier number" (currently, a "CFTC Interim Compliance

Identifier” or “CICI”) to maintain its existing hedges in compliance with Dodd-Frank; (ii) adhere to certain industry standard documents prepared by the International Swaps and Derivatives Association, Inc., known as the “Dodd-Frank Protocols” which, among other things, amend and supplement the District’s hedge documents with counterparties, to be able to enter into new hedges or modify, novate or terminate existing hedges; and (iii) use the “end-user exception” to regulatory requirements that certain hedges be exchange-traded and centrally cleared, to enter into certain new over-the-counter hedges after specified regulatory compliance dates.

The District’s Chief Financial/Risk Officer and staff recommend that the Commission adopt the proposed Amended and Restated Interest Rate Hedge Policy, approve adherence to the Dodd-Frank Protocol documents, including taking all actions incidental thereto, and use of the end-user exception. The General Manager concurs with this recommendation.

#### **ACTION**

IT IS RESOLVED BY THE COMMISSION OF PUBLIC UTILITY DISTRICT NO. 1 OF CHELAN COUNTY, WASHINGTON, as follows:

Section 1. Findings of the Commission. The Commission hereby finds it to be in the District’s best interest to adopt the Amended and Restated Interest Rate Hedge Policy attached hereto as Exhibit A and that such Policy supports the District’s Strategic Plan to develop and implement policies to assure financial stability for the long term.

Section 2. Amended and Restated Interest Rate Hedge Policy. The Commission hereby adopts the Amended and Restated Interest Rate Hedge Policy attached hereto as Exhibit A. The Amended and Restated Interest Rate Hedge Policy supersedes and replaces all prior versions of the District’s Interest Rate Hedge Policy.

Section 3. Dodd-Frank Protocols. The Commission hereby authorizes and directs the General Manager (or designee) to execute and deliver or cause to be delivered each of the Dodd-Frank Protocol documents, in such form as the General Manager, or designee, may approve, such approval to be conclusively evidenced by the execution and/or delivery thereof.

Section 4. Legal Entity Identifier; Other Filings and Registrations; Amendment of Hedge Documents. The Commission hereby authorizes and directs the General Manager (or designee) to take all other actions, including without limitation, to make all filings or registrations required in connection with the provisions of Dodd-Frank, including filing for a legal entity identifier (currently, a CFTC Interim Compliant Identifier, the filing for which is hereby ratified and approved), and hereby approves any amendments to existing hedge documentation relating to the requirements of Dodd-Frank as may be agreed to with a hedge counterparty and of the taking of any other action deemed necessary or desirable to further the purposes of this Resolution.

Section 5. End-User Exception. The Commission hereby authorizes and directs District staff to utilize the End-User Exception as authorized by Dodd-Frank in connection with interest rate transactions subject to a mandatory clearing requirement by the Commodity Futures Trading Commission.

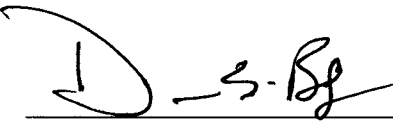
Section 6. Effectiveness. This Resolution shall take effect upon its adoption.

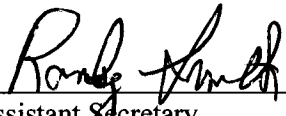
Dated this 19th day of August 2013.

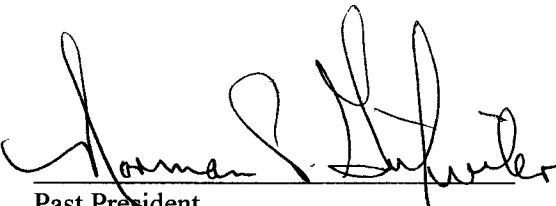
  
\_\_\_\_\_  
President

ATTEST:

\_\_\_\_\_  
Vice President

  
\_\_\_\_\_  
Secretary

  
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Assistant Secretary

  
\_\_\_\_\_  
Past President

SEAL

## I. INTEREST RATE HEDGE POLICY

### 1.0 INTRODUCTION

This Interest Rate Hedge Policy (the "Policy") applies to all Public Utility District No. 1 of Chelan County (the "District") interest rate management agreements, including, but not limited to, interest rate swaps, swaptions, rate locks, forward bond purchase agreements, caps, collars and floors (collectively "Hedges") executed in connection with, or incidental to, the issuance, incurring or carrying by the District of specific bonds, notes, bond anticipation notes, commercial paper or other obligations for borrowed money, or lease, installment purchase or other similar financing agreements or certificates of participation in such agreements ("Obligations"). This Policy is prepared in accordance with the Government Finance Officers Association's 2010 Advisory and prior pronouncements regarding the development of a derivatives policy, and conforms to requirements under the Revised Code of Washington ("RCW") 39.96.

### 2.0 PURPOSE

The purpose of this Policy is to establish guidelines for the use and management of all Hedges. The Policy sets forth the manner of execution of Hedges, and provides for security and payment provisions, risk considerations and certain other relevant provisions. All Hedges must be consistent with the District's overall debt management strategy. The failure by the District to comply with any provision of this Policy shall not affect the validity of any Hedges that are otherwise duly authorized and executed.

### 3.0 SCOPE

This Policy shall apply to any Hedge that the District may execute related to interest rate exposure with respect to Obligations. The Policy does not apply to any Hedges related to power marketing or investment activity.

### 4.0 AUTHORITY

The District is authorized to enter into payment agreements under RCW 39.96.

The Chief Financial Officer of the District ("CFO") is the designated administrator of the Policy and shall have the day-to-day responsibility and authority for structuring, implementing, and managing Hedges. The CFO and the General Counsel of the District, in consultation with the District's bond counsel, shall determine whether a proposed Hedge complies with state law and any applicable provisions of the District's resolutions and agreements with respect to its Obligations.

The Board of Commissioners (the "Board") shall authorize by motion or resolution all Hedges and any related documents and agreements.

### 5.0 USE OF INTEREST RATE HEDGES

The District may consider the use of Hedges in connection with the issuance, incurrence or carrying of Obligations and consistent with the District's overall debt management strategy as a means of reducing exposure to interest rate fluctuations, lowering expected net borrowing costs,

and/or increasing budgetary certainty associated with net debt-related costs. Additionally, the District will strive to use Hedges only after an analysis of the economic benefit of the interest rate derivative market in relation to traditional financing methods has been undertaken and indicates a significant financial economic or cost volatility management benefit without excessive levels of additional risk.

Hedges will not be used for speculation – that is, the taking of additional risks unrelated to the District’s business in an effort to provide an economic gain.

The District staff will comply with state law regarding the use of Hedges as well as applicable disclosure requirements as specified by the Governmental Accounting Standard Board (“GASB”).

## **6.0 CONDITIONS FOR THE USE OF INTEREST RATE HEDGES**

### **6.1. Maximum Notional Amount**

The District will limit the total notional amount of outstanding Hedges based on criteria set forth in this Policy regarding the proper management of risks and calculation of termination exposure.

### **6.2. Call Option Value Considerations**

When considering the relative advantages of a proposed Hedge versus traditional fixed rate Obligations, the Board will take into consideration the value of any call option on fixed-rate Obligations.

### **6.3. Financial Advisory Opinion**

On or prior to the date of execution of any Hedge, the District shall obtain a written certification from an independent Financial Advisor that (i) the terms and conditions of the Hedge and any ancillary agreements, including without limitation, the interest rate or rates and any other amounts payable thereunder, are commercially reasonable in light of then-existing market conditions; and (ii) the Hedge, if fully performed by all parties thereto, will either reduce the amount or duration of the District’s exposure to changes in interest rates or results in a lower net cost of borrowing with respect to the related Obligations.

### **6.4 Financial Advisor Criteria**

“Financial Advisor” shall mean a financial services or financial advisory firm meeting the requirements of the RCW 39.96:

- with recognized knowledge and experience in connection with the negotiation and execution of Hedges;
- that is acting solely as financial advisor to the District in connection with the execution of the Hedge and the issuance or incurring of any related Obligations, and not as a principal, placement agent, purchaser, underwriter, or other similar party, and that does not control, nor is it controlled by or under common control with, any such party;
- that is compensated for its services in connection with the execution of Hedges, either directly or indirectly, solely by the District;

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- that agrees to comply with each of the requirements for Financial Advisors set forth in Section 16.1 of this Policy; and
- whose compensation is not based on a percentage of the notional amount of the Hedge or of the principal amount of any related Obligations.

**7.0 INTEREST RATE HEDGE AGREEMENT FEATURES**

**7.1. Interest Rate Hedge Agreements**

The District will use terms and conditions as set forth in the International Swap and Derivatives Association, Inc. ("ISDA") Master Agreement with modifications as appropriate to enhance the security and position of the District. The Hedge agreement (the "Hedge Agreement") between the District and each counterparty shall include payment, term, security, collateral, default, remedy, termination, and other terms, conditions, provisions and safeguards as the District deems necessary or desirable.

Subject to the provisions contained herein, the terms of any proposed Hedge Agreement shall use the following guidelines:

- Downgrade provisions with respect to the District triggering termination should be no higher than BBB.
- Downgrade provisions with respect to the counterparty or its guarantor triggering termination should be no lower than BBB-.
- To the extent not inconsistent with RCW 39.96, governing law for Hedge Agreements should be the State of New York. Issues relating to jurisdiction, venue, waiver of jury trial and sovereign immunity will be subject to prevailing law. Preference will be given to language providing that the Hedge counterparty will consent to non-exclusive jurisdiction in Federal Courts in Washington with respect to enforcement of the Agreement.
- There should be no right of set-off.
- Collateral thresholds for the Hedge counterparty should be reflective of credit ratings. Collateral requirements should be established and based upon the credit ratings of the Hedge counterparty or guarantor.
- Eligible collateral should be limited to U.S. cash, Treasuries and obligations of Federal Agencies where the principal and interest are guaranteed by the United States.
- The District should have the right to optionally terminate a Hedge at a market price determined in accordance with the terms of the Hedge Agreement at any time over the term of the Hedge.
- Termination value should be set by a "Market Quotation" and "Second Method," (for a 1992 ISDA Master Agreement) or "Close-out Amount" (for a 2002 ISDA Master Agreement), unless the District deems an alternative methodology appropriate.

**7.2. Qualified Hedge Counterparties**

**7.2.1. Credit Criteria**

The District shall be authorized to enter into Hedges only with the following counterparties:

- i. The counterparty has a rating from at least two nationally recognized credit rating agencies, as of the date of execution of the Hedge, that is within the two highest long-term investment grade rating categories, without regard to subcategories; or
- ii. The payment obligations of the counterparty are unconditionally guaranteed by an entity that then has the ratings set forth in (i) above; or
- iii. (1) The counterparty has a rating from at least two nationally recognized credit rating agencies, as of the date of execution of the Hedge, that is within the three highest long-term investment grade rating categories, without regard to subcategories, and (2) the payment obligations of the counterparty are collateralized by either U.S. cash or direct obligations of, or obligations the principal and interest on which are guaranteed by, the United States of America, that (a) are deposited with the District or an agent of the District; and (b) maintain a market value of not less than 102 percent of the net market value of the Hedge to the District, as such net market value may be defined and determined from time to time under the terms of the Hedge; or
- iv. The payment obligations of the counterparty are unconditionally guaranteed by an entity that then has the ratings set forth in (iii) above; and the payment obligations of the counterparty are collateralized as set forth in (iii) above; and
- v. Each counterparty or its guarantor shall have a minimum capitalization of at least \$250 million at the time of execution of the Hedge.

If the District enters into a Hedge with a counterparty described in (i) or (ii) above, the Agreement shall provide that, in the event the credit rating of the counterparty or its guarantor falls below the level required in (i) and (ii) above, as applicable, the counterparty will comply with the collateralization requirements set forth in (iii) or (iv) above.

In addition to the rating criteria specified herein, the District may seek additional credit enhancement and safeguards in the form of:

- Collateral consistent with the policies contained herein;
- Ratings downgrade triggers for termination; and
- A guarantor with a rating from at least two nationally recognized credit rating agencies, as of the date of execution of the Hedge, that is within the two highest long-term investment grade rating categories.

#### 7.2.2. Counterparty Termination Exposure

In order to diversify the District's counterparty credit risk, and to limit the District's credit exposure to any one counterparty, the following guidelines are established for each Hedge counterparty based upon both the credit rating of the counterparty as well as the relative level of risk associated with each existing and proposed Hedge. The guidelines below provide general net termination exposure limits with respect to an initial or additional Hedge with a counterparty. The District may make exceptions to

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the guidelines at any time to the extent that the execution of a Hedge achieves one or more of the goals set forth in this Policy or provides other benefits to the District.

These guidelines shall not require automatic termination of a Hedge or Hedges by the District or the counterparty if the limitations are exceeded during the term of a Hedge. These provisions shall only serve as guidelines in making a determination as to whether or not a proposed Hedge should be executed given the existing and projected levels of net termination exposure to a specific counterparty under all existing and proposed Hedges. Collateral posting guidelines are set forth in the "Collateral" section below. The calculation of Net Termination Exposure (as defined below) with respect to a counterparty shall take into consideration all Hedges with such counterparty, some of which may offset the overall exposure to the District.

The sum of the current market values (positive or negative) of any existing Hedges and the projected exposure under a proposed Hedge shall constitute the Net Termination Exposure with respect to such counterparty. For outstanding transactions, current exposure will be based on the market value as of a date within 30 days prior to the proposed date of execution of the proposed Hedge. Projected exposure shall be calculated based on the Hedge's potential future termination value taking into account possible adverse changes in interest rates as implied by historical or projected measures of potential rate changes applied over the remaining term of the Hedge. The calculation of projected exposure shall be based upon a 2 standard deviation change in the relevant interest rate swap rate, or other such method as the CFO determines reasonably estimates the projected exposure.

The following exposure limits shall be reviewed periodically by the District. If a counterparty has more than one rating, the lowest rating will govern for purposes of calculating the level of exposure.

<b>Counterparty Credit-Based Exposure Limits</b>			
<b>Credit Ratings</b>	<b>Net Collateralized Exposure Limit</b>	<b>Net Uncollateralized Exposure Limit</b>	<b>Aggregate Net Termination Exposure Limit</b>
Aaa/AAA	NA	\$50.0 million	\$50.0 million
Aa/AA Category	\$40.0 million	\$20.0 million	\$60.0 million
A/A Category	\$25.0 million	\$10.0 million	\$35.0 million
Below A3/A-	None	None	None

If the exposure limit is exceeded by counterparty during the term of any Hedge or Hedges, the District shall conduct a review of the exposure limit per counterparty. The District, in consultation with its Bond Counsel and Financial Advisor, shall explore remedial strategies, including but not limited to partial terminations and novations, to mitigate this exposure.

### 7.2.3. Aggregate Net Termination Exposure



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As of the date of entering into any Hedge, the Net Termination Exposure for all the District's existing and proposed Hedges, as determined by the CFO, shall not exceed \$50 million.

7.3. Term and Notional Amount

The notional amount of a Hedge shall not exceed the aggregate principal amount of the Obligations with respect to which the Hedge is executed. The term of a Hedge shall not exceed the final term of the obligation with respect to which the Hedge is made. The District shall not enter into any Hedge that, as of the date of execution, would cause:

- The aggregate net notional amount of all the District's Hedges to exceed 35% of the aggregate principal amount of the District's outstanding Obligations; or
- The District's net exposure to variable interest rates with respect to its outstanding Obligations, including both natural and synthetic variable rate instruments, to exceed 30% of the aggregate principal amount of the District's outstanding Obligations.

7.4. Collateral Requirements

All Hedge Agreements shall provide that if a counterparty (or a guarantor to the counterparty) to the Agreement falls below the two highest long-term investment grade rating categories without regard to subcategories, the party under the Agreement shall collateralize its payment obligations by either U.S. cash or direct obligations of, or obligations the principal and interest on which are guaranteed by, the United States of America, that (a) are deposited with the District or agent of the District; and (b) maintain a market value of not less than one hundred two percent of the net market value of all hedges under the Hedge Agreement to the District, as such net market value may be defined and determined from time to time under the terms of the Hedge Agreement.

Collateral pledged to the District shall be pledged solely to the District. Collateral shall be provided so that the District's security interest in the collateral is perfected, and the collateral is not subject to preference recapture or to a stay in the event of the bankruptcy or insolvency of the Hedge counterparty.

In connection with any collateralization requirements that may be imposed upon the District in connection with entering into a Hedge, the District may post collateral, or may secure liquidity support, or obtain municipal swap insurance or other credit enhancement to secure the timely payment of the District's obligations under the Hedge in lieu of posting collateral. The CFO shall make recommendations regarding collateralization requirements to the Commission with respect to each proposed Hedge.

7.5. Security and Source of Repayment

The District may use the same security and source of payment for Hedges as is used for the Obligations with respect to which the Hedge is executed, but shall consider the economic costs and benefits of subordinating the District's periodic payments and/or termination payments under the Hedge to the Obligations. Bond Counsel shall be consulted regarding the legal requirements associated with making the payments under the Hedge on a parity or subordinate basis with outstanding District Obligations.

The District shall consider the net benefits of using municipal swap insurance, to the extent the same is available from a responsible insurer at a reasonable cost, or other credit enhancement to secure the payment obligations of the District under the Hedge Agreement and to mitigate both termination risk and the necessity of posting collateral if the District's credit rating is lowered.

#### **8.0 COUNTERPARTY SELECTION**

The District may use a competitive or a negotiated process to select a Hedge counterparty and to price a Hedge depending, among other things, on business, market or competitive conditions, provided, that the District shall solicit and give due consideration to proposals from at least two counterparties. Such solicitation and consideration shall be conducted in such manner as reasonably determined by the CFO. The conditions under which a negotiated selection may be used include the following:

- Marketing of the Hedge will require complex explanations about the security for payment or credit quality
- There is limited demand from prospective Hedge counterparties
- Market timing is important, such as for refundings
- Coordination of multiple components of the financing is required
- The Hedge will have non-standard features, such as a forward starting swap
- Municipal swap insurance or other credit enhancement is not available at a reasonable cost
- The notional amount for the Hedge is particularly large
- Counterparties are likely to demand individual changes in bid documents
- Doing so will promote the District's interests in encouraging and rewarding service and the presentation of innovative ideas

#### **9.0 PROHIBITED INTEREST RATE HEDGES**

The District will not use Hedges that:

- are speculative or create extraordinary leverage or risk;
- lack adequate liquidity to terminate without incurring a significant bid/ask spread; and/or
- provide insufficient price transparency to allow reasonable valuation.

#### **10.0 EVALUATION METHODOLOGY**

Prior to Board authorization of a Hedge transaction, the CFO, the District's Financial Advisor and Bond Counsel will provide a summary of the risks and benefits of the proposed transaction. As a part of this review, the District shall compute the projected Net Termination Exposure to the proposed Hedge counterparty. The summary will include an evaluation of at least the following risks and the application of mitigation strategies.

- **Interest rate risk** is created by the exposure to changes in prevailing interest rates.
- **Basis risk** is the mismatch between actual variable rate debt service and variable rate indices used to determine Hedge payments. This risk can be managed through the creation of an interest rate reserve fund or conservative budgeting strategies.

- **Tax risk** is created by potential tax events that could affect Hedge payments, such as changes in the tax-exemption of interest on District Obligations.
- **Counterparty risk** is the potential failure of the counterparty to make required payments under the Hedge Agreement. This risk can be mitigated through the establishment of exposure limits, ratings thresholds, and collateralization requirements.
- **Termination risk** is the potential for termination of the agreements by the counterparty due to market or credit factors. The District may consider purchasing municipal swap insurance or other credit enhancement as a mitigation strategy.
- **Amortization risk** is created when there is a mismatch of amortization schedules as between the notional amount of the Hedge and the principal amount of the related Obligations. This risk can be eliminated when Hedge amortization schedules are established to match the principal amortization of the related Obligations.
- **Collateralization risk** is presented if market movements or a District downgrade causes the market value of the swap to change such that the District is required to post collateral under the terms of the Hedge Agreement.
- **Liquidity risk** is the potential need for significant available funds in order to make required scheduled, collateral or termination payments, particularly on short notice.
- **Accounting risk** is the potential that a Hedge will be subject to treatment for financial reporting purposes that would have an adverse effect on the District's financial statements or on the District's rate covenant compliance.
- **Rollover risk** is the mismatch of the maturity of the Hedge and the maturity of the related Obligations, potentially leaving the District unable to replace the Hedge on terms as favorable as the original Hedge Agreement. This risk can be eliminated by making the Hedge coterminous with the final maturity of the related Obligations.
- **Market access risk** is the risk that the District will be unable to access the debt market and/or related credit enhancement such as a line or letter of credit in the future as may have been assumed when executing some types of Hedges (such as forward starting Hedges). This risk can be mitigated by prudent financial management and potential use of forward municipal bond and swap insurance or other credit enhancement.
- **Credit Facility/Remarketing risk** is evident when an issuer cannot secure a cost-effective renewal of a Letter or Line of Credit or suffers a failed remarketing on variable rate bonds that underlying a floating-to-fixed rate swap. A general mitigation technique is the prudent management of financial resources and bank credit facilities.
- **Credit risk** is the occurrence of an event that impacts the credit rating of the issuer or its counterparty. This can be mitigated through minimizing cross defaults, collateralization, the use of hedge insurance and favorable terms for credit event triggers in the Hedge Agreements.
- **Operational risk** is the potential for mismanagement of an outstanding Hedge through failure to make payments or deliver collateral under such Hedges or to monitor and respond to price changes and interest rate changes, or improper accounting and budgetary treatment. This risk can be mitigated by thorough Hedge policies and detailed periodic reporting to the Board.

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**11.0 MANAGING INTEREST RATE HEDGE RISKS**

11.1. Reporting

The CFO will monitor and evaluate the risks associated with outstanding Hedges on an ongoing basis at least semi-annually and provide a written report to the Board. The report shall include:

- a description of all outstanding Hedges, including notional amount, average life and current Net Termination Exposure of each Hedge;
- net impact to the District of a 100 basis point (1.00%) movement (up or down) in the appropriate interest rate index or yield curve;
- the actual payments for each Hedge, versus the projected payments on the Hedge transaction; and for any Hedges used as part of a refunding, the actual cumulative savings versus the projected savings at the time the Hedge was executed;
- the current credit rating of each Hedge counterparty, parent, guarantor and credit enhancer insuring Hedge payments, if any;
- actual collateral posting by Hedge counterparties, if any, by Hedge Agreement and in total by each Hedge counterparty;
- actual collateral posting by the District, if any, by Hedge Agreement and in total;
- information concerning any material event involving outstanding Hedge Agreements, including a default by a Hedge counterparty, a counterparty downgrade or a termination;
- an updated contingency plan to replace a Hedge counterparty or fund a termination payment in the event an outstanding Hedge is terminated;
- the status of any credit or liquidity support used in connection with Hedges or the related Obligations, including the remaining term and current fees;
- a summary of any proposed Hedges and the projected financial effects of such Hedges on the District.

11.2. Active Management

The District will seek to maximize the benefits it accrues and minimize the risks it bears by actively managing its Hedge program. This will entail continuous monitoring of market conditions in conjunction with the Hedge counterparty and the District's Financial Advisor for emerging opportunities or risks. Active management may entail modification of existing transactions, including:

- early termination of a Hedge Agreement;
- shortening or lengthening the term of a Hedge Agreement;
- sale or purchase of options; and
- the use of Hedges to mitigate basis risk.

**12.0 AMENDING OR TERMINATING INTEREST RATE HEDGES**

12.1. Amendment/Optional Termination

Through the active management of the Hedge program and compliance with District Financial Policies, it may become necessary or desirable to immediately take action related to outstanding Hedge transactions to reduce or mitigate risks that may emerge. In cases where such action is necessary or desirable, in the determination of the District's General Manager, to protect the interests of the District, the District's General Manager (including the acting General Manager in his absence), in consultation with the District's Financial Advisor and Bond Counsel, is authorized to:

- 1) amend an outstanding Hedge or hedge Agreement to comply with either (i) Federal or State laws and/or regulations or (ii) where not so amending would reduce or eliminate the District's ability to transact, amend, novate or terminate Hedges;
- 2) terminate an outstanding Hedge in accordance with its terms;
- 3) pay or finance any termination amount that may consequently be due from the District to a counterparty from available funds of the District; and/or
- 4) enter into one or more replacement Hedges on terms consistent with this Policy.

The General Manager, or his or her designee, is also authorized to execute and deliver such documents, agreements and certificates to accomplish any of the foregoing. The General Manager will provide a formal report of the circumstances and any actions taken to the Board at the next regularly scheduled Board meeting.

#### 12.2. Mandatory Termination

In the event a Hedge is terminated as a result of a termination event, such as a default by or a decrease in credit ratings of the counterparty, the Board will evaluate whether it is financially advantageous to obtain a replacement Hedge, or to make or receive a termination payment.

#### 12.3 Liquidity

The District shall seek to maintain sufficient liquidity, including without limitation through balances in the District's Contingency Account, commercial paper capacity, other borrowing capacity and/or available working capital, to make any Hedge termination payments that may become due, to the extent not paid or payable from other sources.

### **13.0 HEDGE ACCOUNTING TREATMENT**

The District shall comply with any applicable accounting standards with respect to the treatment of agreements allowed under this Policy. The CFO and the Financial Advisor shall implement the applicable accounting standards in connection with the preparation of the District's financial statements and the District's external auditors shall review the accounting treatment of said agreements in the financial statements.

### **14.0 FINANCIAL DISCLOSURE**

The District will ensure that there is appropriate disclosure of all Hedges to rating agencies and in disclosure documents with respect to its Obligations. Disclosure in documents, including offering documents for any Obligations, shall provide a summary of any special risks with respect to any Hedges.

## 15.0 POLICY AMENDMENT

Annually, the CFO will review this policy and, if appropriate, propose any desired amendments to the policy for approval by the Board.

The District reserves the right to modify this Policy at such times and for such purposes as such modifications may more effectively advance its debt management objectives.

## 16. DODD-FRANK ACT

### 16.1 Conformance to Dodd-Frank

It is the intent of the District to conform this Policy to the requirements relating to legislation and regulations for derivatives transactions under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, as supplemented and amended from time to time, including any regulations promulgated in connection therewith (herein collectively referred to as “Dodd-Frank”). Pursuant to such intent, it is the policy of the District that, with respect to each Hedge: (i) each Financial Advisor engaged or to be engaged by the District will function as the designated qualified independent representative of the District, sometimes referred to as the “Designated QIR”; (ii) each Financial Advisor agree to meet and meets the requirements specified in Commodity Futures Trading Commission (“CFTC”) Regulation 23.450(b)(1) (17 C.F.R. 23.450(b)(1)) or any successor regulation thereto (herein referred to as the “Representative Regulation”); (iii) each Financial Advisor provide a written certification to the District to the effect that such Financial Advisor agrees to meet and meets the requirements specified in the Representative Regulation; (iv) the District monitor the performance of each Financial Advisor consistent with the requirements specified in the Representative Regulation; (v) the District exercise independent judgment in consultation with its Financial Advisor in evaluating all recommendations, if any, presented by any swap dealer with respect to transactions authorized pursuant to this Policy; and (vi) the District rely on the advice of its Financial Advisor with respect to Hedges authorized pursuant to this Policy and not rely on recommendations, if any, presented by any swap dealer with respect to Hedges authorized pursuant to this Policy.

### 16.2 Legal Entity Identifier

The District shall obtain and maintain current at all times a “legal entity identifier” from a firm designated by the CFTC to provide such numbers.

### 16.3 Clearing

In connection with the execution of any Hedge that is subject to a mandatory clearing requirement by the CFTC, the District shall complete and maintain, as required by the CFTC, an annual filing regarding how it generally meets its financial obligations associated with entering into uncleared Hedges to satisfy the requirements of the “End-User Exception to the Clearing Requirement for Swaps” rule as specified in CFTC Regulation 17 C.F.R 39.6.

### 16.4 Recordkeeping

Comprehensive records shall be maintained, either in paper or electronic form, of any Hedge entered into by the District for at least five (5) years following the termination thereof. Such records shall be retrievable within five (5) business days and shall be open to inspection by the CFTC.

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16.5 Swap Dealers

Each counterparty with which the District executes a Hedge will be registered with the CFTC as a “swap dealer” and will, among other things, be responsible for all reporting requirements under the Commodity Exchange Act, as amended.