

976 CMR: STATE FINANCE AND GOVERNANCE BOARD

976 CMR 2.00: STATE FINANCE AND GOVERNANCE BOARD REGULATIONS

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2.01: Purpose and Application

The powers and responsibilities of the Board set forth in M.G.L. c. 6, § 98 are intended to promote transparency, accountability and best practices among State Entities with respect to investments, borrowing or other financial transactions involving public funds made or entered into by State Entities.

2.02: Definitions

For purposes of 976 CMR 2.00, the following definitions shall apply, in addition to the definitions appearing in M.G.L. c. 6, § 97:

Board. The State Finance and Governance Board, established under M.G.L. c. 6, § 97.

Commonwealth. The Commonwealth of Massachusetts.

Derivative Financial Product. Any financial instrument which is a bond or note issue of a State Entity Authorized to Issue Debt or which is related to a bond or note issue of a State Entity Authorized to Issue Debt the value of which is derived from or based upon the value of other assets or on the level of an interest rate index including, but not limited to, a call option on a bond, interest rate swap agreements, interest rate swaptions, caps, floors, collars, inverse floaters and auction rate securities; provided, however, that any bonds or notes issued by State Entities Authorized to Issue Debt with fixed rates of interest shall not constitute Derivative Financial Products, regardless of whether such fixed rate bonds or notes are issued with a call option, regardless of whether such fixed rate bonds or notes are insured by bond insurance or other form of credit enhancement, and regardless of investment or lending of such fixed rate bond or note proceeds.

Public Funds. Any funds that are received by a State Entity Authorized to Issue Debt from the Commonwealth or any other public or private source, and are under the control of and are expended at the discretion of the State Entity Authorized to Issue Debt.

Qualified Conduit Debt Transaction. Any issue of bonds or notes issued by a State Entity Authorized to Issue Debt acting in a conduit role for a non-governmental, for-profit or non-profit corporation or group of related or unrelated for profit or non-profit corporations (none of which is itself a State Entity Authorized to Issue Debt) (collectively, the borrower), and any derivative financial products related to such issue, which are secured by and payable by the borrower, a related guarantor, or any third party guarantee such as a letter of credit or bond insurance. Such bonds or notes, or related derivative financial products, shall not be payable under any circumstances from public funds of, and shall not be the liability of, the State Entity Authorized to Issue Debt that issued the bonds or notes, the Commonwealth or any other State Entity Authorized to Issue Debt.

Qualified Conduit Debt Transaction with Guarantee. Qualified Conduit Debt Transaction for which there is a related guarantee provided by the State Entity Authorized to Issue Debt acting in a conduit role.

State Entity. The Commonwealth, any state authority as defined in M.G.L. c. 29, § 1, or other state entities of the Commonwealth with responsibility for managing and overseeing Public Funds.

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State Entity Authorized to Issue Debt. Any State Entity with authority to issue bonds or notes, including the following currently existing State Entities Authorized to Issue Debt while they continue to exist, and any future State Entities Authorized to Issue Debt that are created by statute and that meet the definition set forth in M.G.L. c. 6, § 97 and 976 CMR 2.00:

Commonwealth of Massachusetts	Massachusetts Clean Water Trust
Massachusetts Bay Transportation Authority	Massachusetts Water Resources Authority
Massachusetts Development Finance Agency	University of Massachusetts Building Authority
Massachusetts Educational Financing Authority	Woods Hole, Martha's Vineyard, Nantucket Steamship Authority
Massachusetts Housing Finance Agency	Regional Transit Authorities
Massachusetts Port Authority	
Massachusetts School Building Authority	
Massachusetts State College Building Authority	
Massachusetts Department of Transportation as successor to Massachusetts Turnpike Authority	

State Entity Authorized to Issue Debt Subject to Waiver Process (SESWP). The meaning set forth in 976 CMR 2.07.

2.03: Policies Relating to Investment of Public Funds

Upon adoption of a substantive revision, a State Entity Authorized to Issue Debt shall file its revised policy or policies related to the investment of Public Funds with the Board.

2.04: Debt Management Policies

Upon adoption of a substantive revision, a State Entity Authorized to Issue Debt shall file its revised policy or policies related to debt management with the Board. The Board shall make the policies filed with it available on its website and to any member of the public upon reasonable request to review.

2.05: Review of Financial Transactions Involving Derivative Financial Products

In furtherance of its statutory authority and mandate, the Board hereby establishes 976 CMR 2.05 to ensure that financial transactions involving a Derivative Financial Product are properly analyzed and managed to ensure consistency with State Entity Authorized to Issue Debt objectives, suitability of the transaction, and avoidance of unintended consequences.

In the event that a State Entity Authorized to Issue Debt is entering into a new financial transaction that involves a Derivative Financial Product, the State Entity Authorized to Issue Debt shall submit the following materials to the Board:

- (1) If not previously submitted, a copy of the State Entity Authorized to Issue Debt's derivative policy* with a certified copy of the vote of the governing board of the State Entity Authorized to Issue Debt or certificate of the authorized official of the State Entity Authorized to Issue Debt if such State Entity Authorized to Issue Debt does not have a governing board; and
- (2) A written analysis of the proposed Derivative Financial Product transaction by an independent financial advisor with relevant expertise, together with the advisor's recommendation as to whether or not the State Entity Authorized to Issue Debt should enter into the proposed transaction. Such analysis should include but not be limited to:
 - (a) a detailed description of the Derivative Financial Product;
 - (b) a description of risks, strategies for mitigating any such risks, and any benefits;

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- (c) scenario analyses or stress tests demonstrating impact on the State Entity Authorized to Issue Debt under extreme financial market events or conditions as a result of entering into the subject Derivative Financial Product; and
- (d) in the case of a restructuring of an existing Derivative Financial Product, a comparison of the expected benefits resulting from the restructuring with the potential risks resulting from the restructuring.

(3) A certified copy of the minutes of the meeting of the governing board of the State Entity Authorized to Issue Debt (such meeting to be held on a date not greater than two years prior to the date of Board review), or a certificate of the authorized official of the State Entity Authorized to Issue Debt, demonstrating or confirming that:

- (a) the written analysis and recommendation of the independent financial advisor was presented to the board, or to the official and transmitted to the board;
- (b) that the structure of the Derivative Financial Product is consistent with the derivative policy adopted by the board or approved by the authorized official;
- (c) that the benefits of the Derivative Financial Product outweigh the risks of the use of a Derivative Financial Product; and
- (d) that the governing board or the official approved the proposed transaction.

* The following issues should be considered in connection with such a policy:

1. How derivative products fit within the overall debt management program;
2. Expected outcomes or goals of entering into a derivative product (*i.e.* synthetically fix a variable rate at lower rate than otherwise available in the market);
3. Security and sources of payments for ongoing costs associated with the derivative product and for termination costs of the derivative product;
4. A list of the types of derivative products that may be used and a list of the types of derivative products that are prohibited;
5. The conditions under which these types of products can be utilized (*i.e.* bidding procedures, minimum benefit thresholds, terms of master agreements, *etc.*);
6. The maximum amount of derivatives contracts, or a means of determining such amount;
7. Guidelines and criteria for selecting counterparties;
8. Methods for evaluating, measuring and managing derivative risk;
9. Methods and process for procuring derivative products;
10. Post issuance monitoring, reporting and ongoing risk mitigation procedures, including periodic valuation.

The Board's review pursuant to 976 CMR 2.00 shall consist of reviewing the items required to be submitted to the Board described in 976 CMR 2.05(3)(d)1. through 10. The Board shall either conclude that the items required to be submitted have in fact been submitted consistent with the purpose and intent of 976 CMR 2.00, or that said items have not been submitted in a manner consistent with the purpose and intent of 976 CMR 2.00. Any conclusion shall be established by vote of the Board, and confirmed in writing (which may be by e-mail) to the State Entity Authorized to Issue Debt. Such conclusion shall be valid unless the State Entity Authorized to Issue Debt informs the Board of any material change in any of the submittals pursuant to 976 CMR 2.05 or unless six months have lapsed from the date of Board conclusion.

A State Entity Authorized to Issue Debt which has received a Board conclusion that the items required to be submitted in connection with 976 CMR 2.00 were in fact submitted consistent with the purpose and intent of 976 CMR 2.00 must report to the Board at the Board meeting next following the execution of the Derivative Financial Product transaction. Such report should include, but not be limited to, the results or final terms of the Derivative Financial Product transaction.

2.06: Review of Qualified Conduit Debt Transactions Involving Derivative Financial Products; with Guarantee

- (1) With respect to any proposed Derivative Financial Products that are related to a Qualified Conduit Debt Transaction, the Board's review of such transaction shall be limited to confirming that the transaction constitutes a Qualified Conduit Debt Transaction.

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(2) In order to request a review of any Derivative Financial Products that are related to a Qualified Conduit Debt Transaction, a State Entity Authorized to Issue Debt must submit the following items to the Board prior to such Derivative Financial Product being executed:

- (a) A written description of the proposed Derivative Financial Product transaction(s), including: the parties involved; the schedule; the amount; the security (including any guarantor of payment obligations); and terms.
- (b) A certification of bond counsel to the proposed transaction confirming that the transaction constitutes a Qualified Conduit Debt Transaction pursuant to 976 CMR 2.06.

Not later than five business days following receipt of the material submitted in connection with any Derivative Financial Product related to a Qualified Conduit Debt Transaction, the Secretary of the Board will contact the State Entity Authorized to Issue Debt in writing (which may be by e-mail) to either:

- 1. confirm that, based on the materials provided under 976 CMR 2.00, the transaction constitutes a Qualified Conduit Debt Transaction and either no public funds are at risk in the transaction or the amount of guarantee, if any, is equal to or less than the threshold amount in 976 CMR 2.06(3); or
- 2. notify the State Entity Authorized to Issue Debt that the materials submitted were incomplete or that they fail to demonstrate that the transaction constitutes a Qualified Conduit Debt Transaction.

(3) With respect to any proposed Derivative Financial Products that are related to a Qualified Conduit Debt Transaction with Guarantee, the Board's review of such transaction shall be the same as the review of Qualified Conduit Debt Transactions Involving Derivative Financial Products as described in 976 CMR 2.06(2), provided that the governing board of the related State Entity Authorized to Issue Debt has delegated authority to its staff to extend such guarantee without further approval based on an established threshold dollar value and/or risk rating of such guarantee as may be determined by the governing board from time to time, or provided that the guarantee is not greater than \$1 million.

- (a) With respect to any proposed Derivative Financial Products that are related to a Qualified Conduit Debt Transaction with Guarantee which does not meet the criteria in 976 CMR 2.06, the Board's review of such transaction shall be the same as review of financial transactions involving Derivative Financial Products as described in 976 CMR 2.05.
- (b) A State Entity Authorized to Issue Debt that issues Qualified Conduit Debt Transactions With Guarantee must submit a periodic (but at least quarterly) report of its guarantee programs (Guarantee Program Report). The Guarantee Program Report shall include, but not be limited to: the number and dollar amount of outstanding guarantees by segregated guarantee program and the change in the number and dollar amount of such guarantees from the prior reporting period; the number and dollar amount of guarantees paid during the reporting period with an explanation of the circumstances surrounding such payments. The Board, in its sole discretion, may request further information about the guarantee program.

2.07: Review of Requests for Waiver from Presumption of a Competitively Bid Financing

Statutorily, the Commonwealth may not sell bonds or notes maturing at a time later than three years from their dates on a negotiated basis without receiving a waiver from the Board. In addition, any State Entity Authorized to Issue Debt for which the Secretary of Administration and Finance approves the sale of its bonds or which issues bonds that receive Commonwealth support to the extent that Commonwealth disclosure is used in the marketing of such bonds, may not sell bonds or notes on a negotiated basis without receiving a waiver from the Board, including but not limited to the University of Massachusetts Building Authority, the Massachusetts State College Building Authority, certain of the Massachusetts Department of Transportation bonds, the Massachusetts Clean Water Trust, the Massachusetts Development Finance Agency as issuer of bonds supported by Commonwealth contract assistance and the Woods Hole, Martha's Vineyard and Nantucket Steamship Authority (together with the Commonwealth, "State Entities Authorized to Issue Debt Subject to Waiver Process" or "SESWP"). In the event that a SESWP seeks to sell bonds or notes on a negotiated basis, the SESWP shall submit the following materials to the Board:

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- (1) If not previously submitted, a copy of the SESWP's Debt Management Policy with a certified copy of the board of the SESWP vote or certificate of the authorized official of the SESWP if such State Entity Authorized to Issue Debt does not have a governing board;
- (2) Certified copy of the minutes of a meeting of the governing board of the SESWP or certificate of the authorized official of the SESWP, evidencing awareness and approval that the SESWP will be selling bonds or notes on a negotiated basis; and
- (3) A letter from an authorized official of the SESWP to the Board and presented at a Board meeting requesting a waiver from the presumption of a competitively bid financing and demonstrating that:
 - (a) the process or criteria to determine the method of sale set forth in the SESWP's Debt Management Policy had been thoroughly followed;
 - (b) an explanation for why the SESWP believes negotiation is a better approach;
 - (c) the date beyond which such waiver, if granted, would expire;
 - (d) a "not-to-exceed" amount of bonds to be sold; and
 - (e) a description of the use of proceeds of the subject bonds or notes. Such letter shall be personally presented to the Board by an appropriate official of the SESWP.

Consistent with statute, the Board's presumption is that SESWP bond sales will be conducted on a competitive basis. There may be exceptions to this premise, however, where the anticipated benefit of a negotiated sale can be demonstrated. The Board's review pursuant to 976 CMR 2.00 shall consist of reviewing the items required to be submitted to the Board as described in 976 CMR 2.07(3)(a) through (e). The Board shall either conclude that the items required to be submitted have in fact been submitted in a manner consistent with the purpose and intent of 976 CMR 2.00 and grant a waiver, or that said items have not been submitted consistent with the purpose and intent of 976 CMR 2.00. Any conclusion shall be established by vote of the Board, and confirmed in writing (which may be by e-mail) to the SESWP. Any conclusion will expire six months from the date thereof.

A SESWP that received a waiver pursuant to 976 CMR 2.00 must present results of the sale, including comparative pricing information, to the Board at the next Board meeting following the execution of the negotiated sale.

2.08: Board Contact Information

Whenever a document is required to be submitted to the Board under 976 CMR 2.00, it shall be submitted to:

State Finance and Governance Board
c/o Director of Debt Management and Special Finance Programs
Executive Office for Administration and Finance
State House, Room 373
Boston, MA 02133

REGULATORY AUTHORITY

976 CMR 2.00: M.G.L. c. 6, § 98.