

## Current Developments in Financing Tax-Exempt Bonds

The logo for SACUBO, featuring the word "SACUBO" in a stylized, blue, serif font with a gold outline. The letters are set against a background of a financial document with a line graph and various numerical values.

SACUBO

October 21, 2008

George Pugh  
Managing Director  
Morgan Keegan & Company, Inc.  
912-634-2824  
[george.pugh@morgankeegan.com](mailto:george.pugh@morgankeegan.com)

**2002-2006**

- Very low interest rates & accommodative monetary policy
- Housing construction occurs at rates much faster than home formations
- Innovative residential financing develops
  - Securitization
  - 100% financing
  - Payment option ARM's
  - Bond insurers participate

**2007**

- Tighter monetary policy
- Housing sales slow
- New construction declines
- Housing prices begin to fall

**2008**

- Mortgage defaults and foreclosures
- Bond insurers lose AAA rating
- Many banks and investment banks experience large write-offs

**Sept./Oct. 2008**

- Fannie and Freddie Nationalized
- Washington Mutual given to JP Morgan
- Lehman Brothers Bankruptcy
- Reserve Prime Money Market Fund “Breaks the Buck”
- Commercial Paper market implodes
- AIG taken over by the U.S. Treasury
- Wachovia experiences run on bank and is sold twice – Citi and Wells
- TARP
- Foreign countries “bail out” many institutions
- Hedge Funds forced to “de-lever”

**Fall 2007**

- Bond insurer problems re: insurance of mortgage securities
- Auction Rate Securities experience failed auctions

**Early 2008**

- More ARS auction failures
- Insured VRDBs are tendered to remarketing agents
- Issuers of ARS and insured VRDBs seek alternate credit/liquidity support
- Synthetic variable rate structures go “upside-down”, flooding secondary market
- SIFMA goes haywire vs. LIBOR
- Issuers with fixed payer swaps forced to pay termination penalty to restructure

**Mid 2008**

- Investors in VRDBs become very selective regarding bank letters of credit
- Letters of credit become more expensive

**Fall 2008**

- Lehman Brothers bankruptcy hits money market funds causing outflows to U.S. Treasuries
- Tax-Exempt money funds see net redemptions
- SIFMA approaches 9%
- Banks experience draws on letters of credit
- Fixed rate tax-exempt bond market is overwhelmed by forced selling of leveraged positions
- Back up liquidity facilities and letters of credit are virtually non-existent for new VRDB issues

## Four of the top ten Underwriters in 2007 will no longer be in the business in 2009

National Long Term Municipal New Issues Full Credit to Book Runner Year Ended 2007			
<i>Rank</i>	<i>Underwriter</i>	<i>Par Amount (US\$ mil)</i>	<i>No. of Issues</i>
1	Citi	61,861.1	603
<del>2</del>	<del>Merrill Lynch &amp; Co</del>	<del>47,927.1</del>	<del>423</del>
<del>3</del>	<del>UBS Securities LLC</del>	<del>36,253.0</del>	<del>613</del>
4	Goldman Sachs & Co	28,003.8	182
5	J P Morgan Securities Inc	25,566.3	338
6	Morgan Stanley	25,495.1	255
<del>7</del>	<del>Lehman Brothers</del>	<del>24,803.9</del>	<del>250</del>
<del>8</del>	<del>Bear Stearns &amp; Co</del>	<del>24,629.8</del>	<del>133</del>
9	Banc of America Securities LLC	17,051.1	402
10	RBC Capital Markets	14,307.8	568
<b>11</b>	<b>Morgan Keegan &amp; Co Inc</b>	<b>11,055.4</b>	<b>556</b>
12	Wachovia Securities	10,684.4	462
13	Piper Jaffray & Co	6,838.8	420
14	George K Baum & Company Inc	6,674.5	269
15	Stone & Youngberg	4,668.1	214

- Bond Insurers Continue Downgrade Trends -
  - MBIA and Ambac Fall From Grace
  - Fitch Withdraws Ratings on MBIA and Ambac
  - FSA and AGA are on Moody's "Negative Watch"
  
- Foreclosure Activity's Impact on Municipal Credit Quality
  
- State and Local Governments Clouded Prospects
  
- Rating Agencies Global Rating Scale
  
- Remembering History - The Hempel Study

- The Year Starts Slowly
- Auction Rate Bond Problems Surface
- Jefferson County Alabama—Sewer Bonds
  - Flawed Debt Mix
- Vallejo California Files for Bankruptcy
  - Labor and Pension Costs
- Insured Municipals Comprise Just 24% of First-Half Issuance

### Municipal Bond Issuance (ended 9/30/08)

<b>Bonds Issued (\$bn)</b>	<b>2008</b>	<b>2007</b>	<b>% Change</b>
<b>Total</b>	317.8	325.2	-2.27%
<b>New Money</b>	167.7	198.9	-15.6%
<b>General Obligations</b>	94.2	100.4	-6.1%
<b>Revenue</b>	223.5	224.8	-0.05%
<b>Taxable</b>	21.9	22.4	-2.23%
<b>Bond Insured</b>	65.0	158.0	-58.9%

Source: Bond Buyer

- Prior to 1929 most Cities and States were rated Aaa or Aa because conventional wisdom at the time treated them like sovereign government (McDonnell Investments 4/14/08).
- According to George Hempel's study, "The Postwar Quality of Municipal Bonds", there were as many as 3,352 total municipal bond defaults at the peak of the Depression in 1935.

Type	Peak Number in Default	Date
States	1-3*	May 1, 1933
Counties	359	July 1, 1934
Cities and Towns	851	January 1, 1935
School Districts	882	August 1, 1935
Other Districts	299	September 1, 1935
Special Purpose & Districts	1173	May 1, 1938

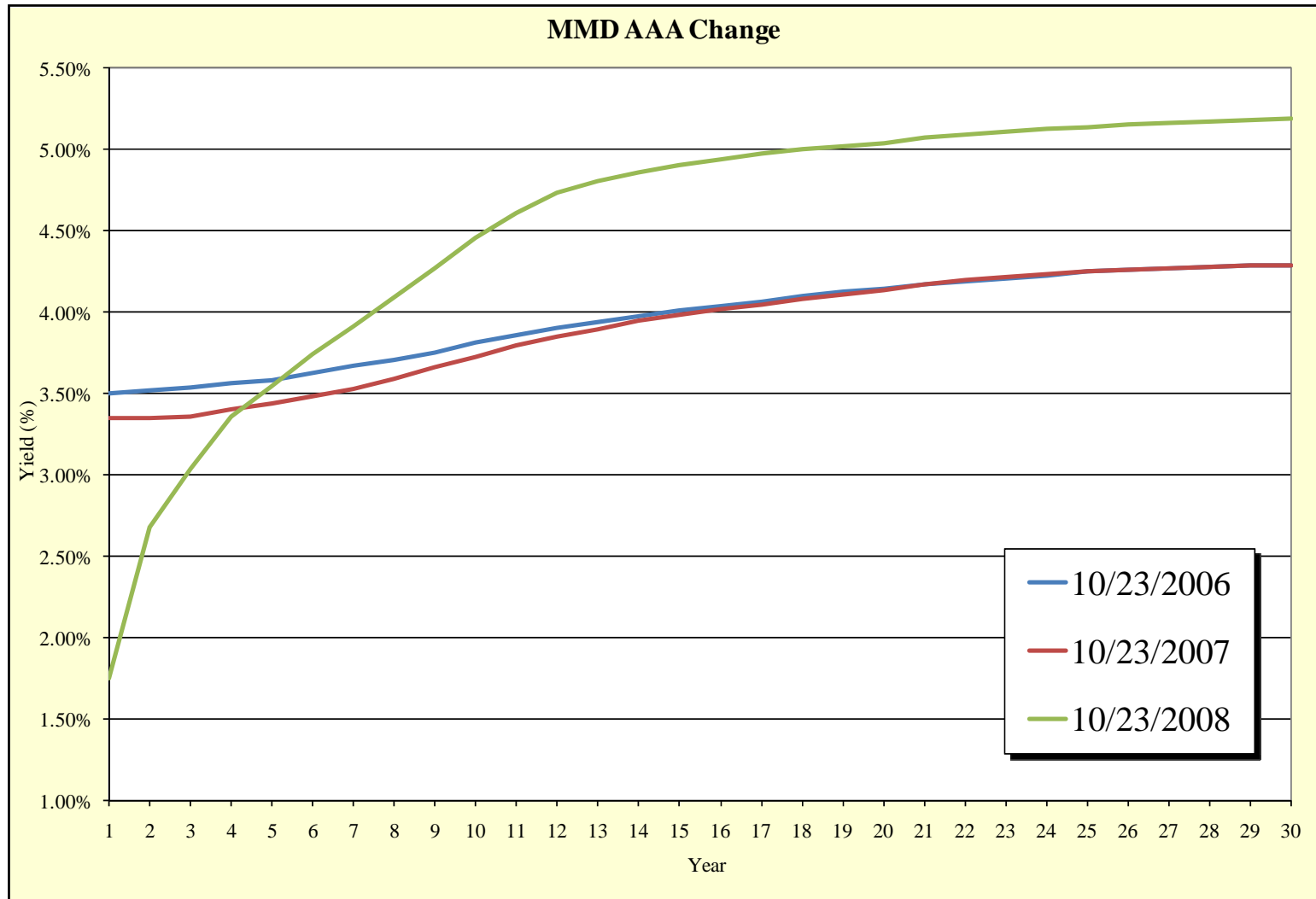
\*Hempel Study questioned whether two of the three states actually defaulted

## The Future of the Tax-Exempt Bond Market

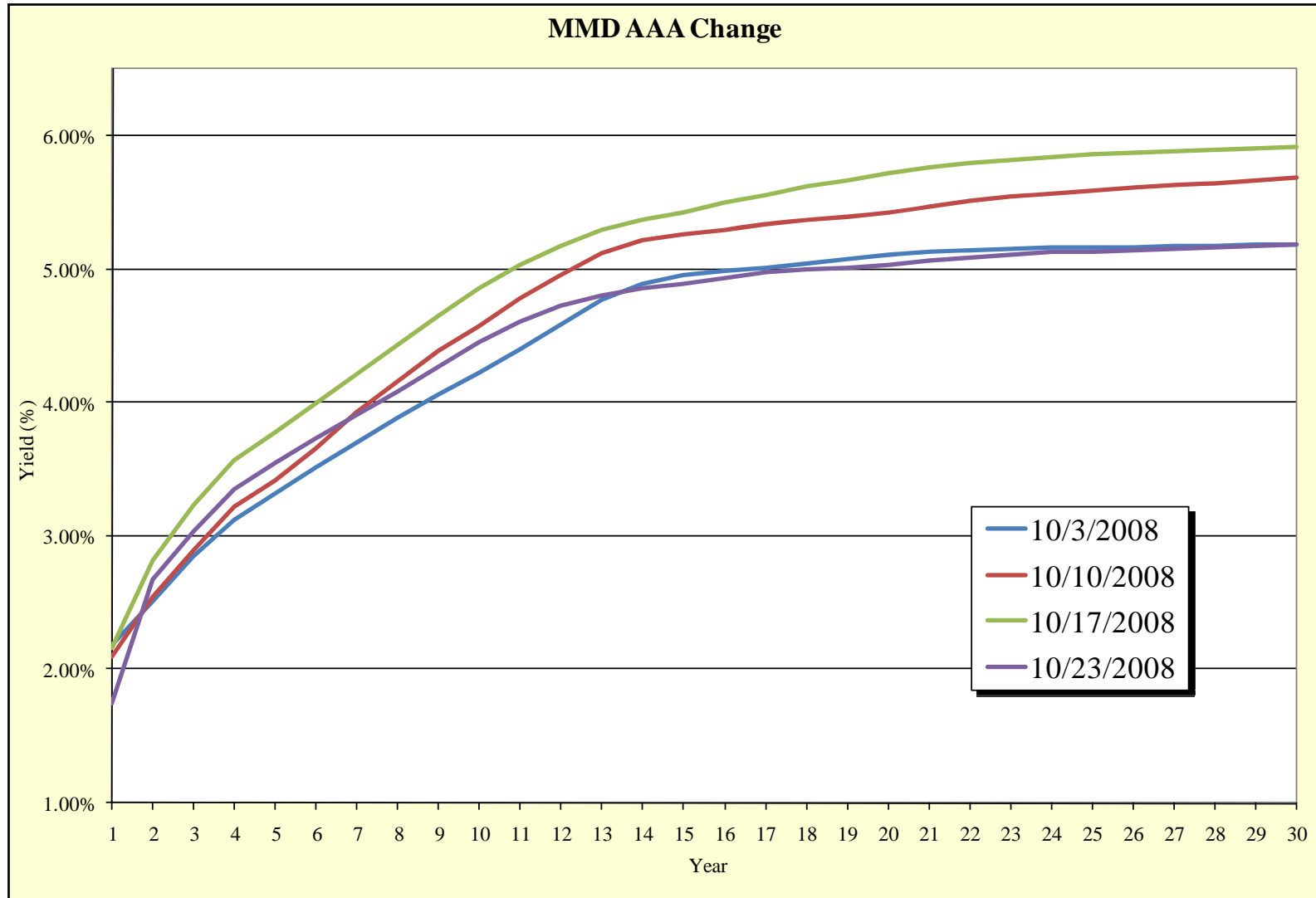
- Liquidity is returning to the short-term credit markets
- New bond insurers are emerging (Berkshire Hathaway, MIAC, Connie Lee)
- Letter of credit banks
  - Fewer players, less aggressive
  - Letters of credit more expensive
- Fewer Public Finance firms
  - Bear Stearns
  - UBS
  - Lehman
  - Merrill
  - Wachovia - in question

} Gone
- Derivatives activity may decline
  - Counterparty risk
  - Basis risk
  - Credit enhancement risk
- Credit will be “KING”; Liquidity a “PRINCE”
- Issuers will prefer traditional fixed rate structures

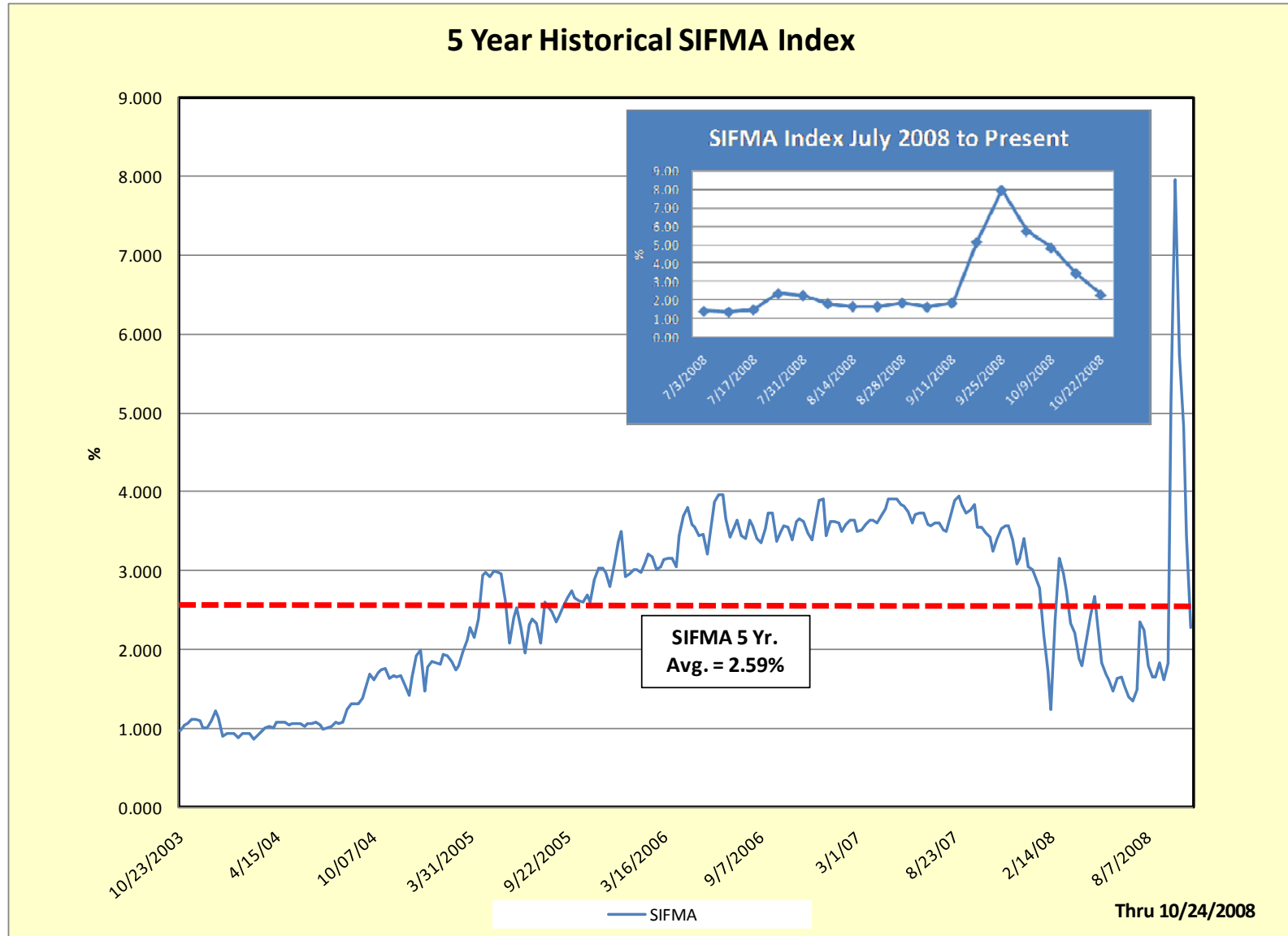
AAA MMD Yield Curve: 3rd Quarter 2006, 2007 & 2008



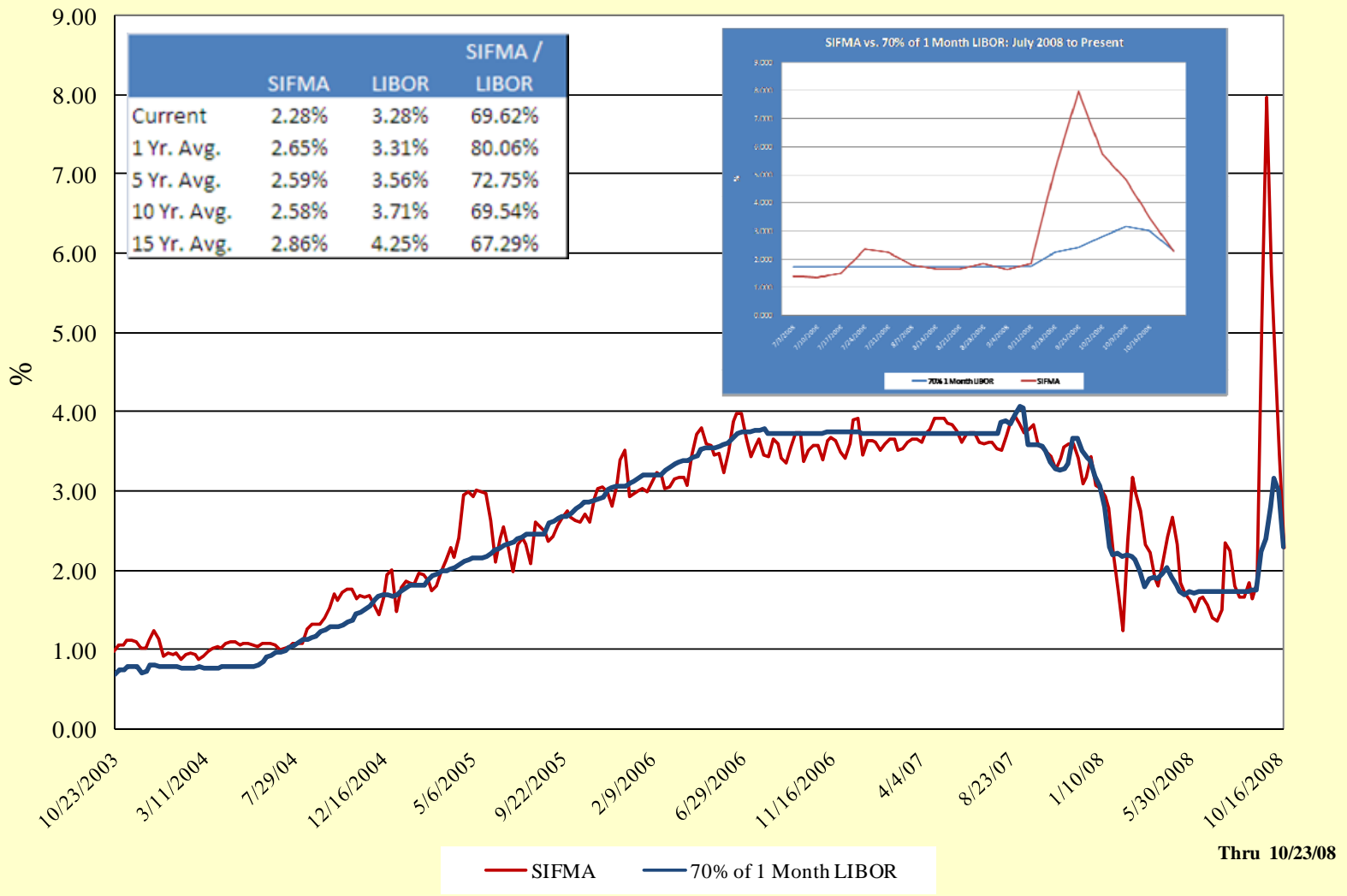
AAA MMD: Last 4 Weeks

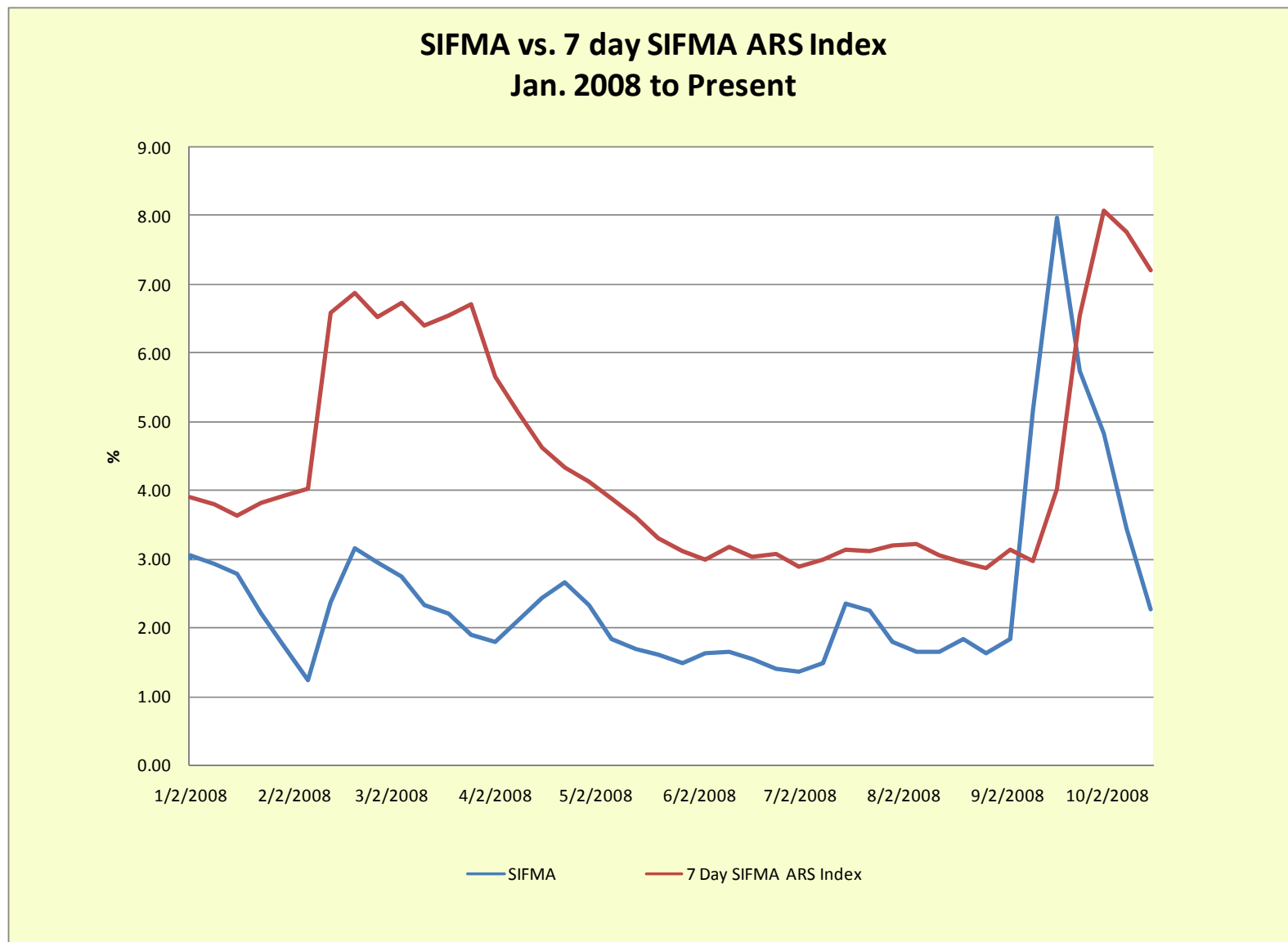


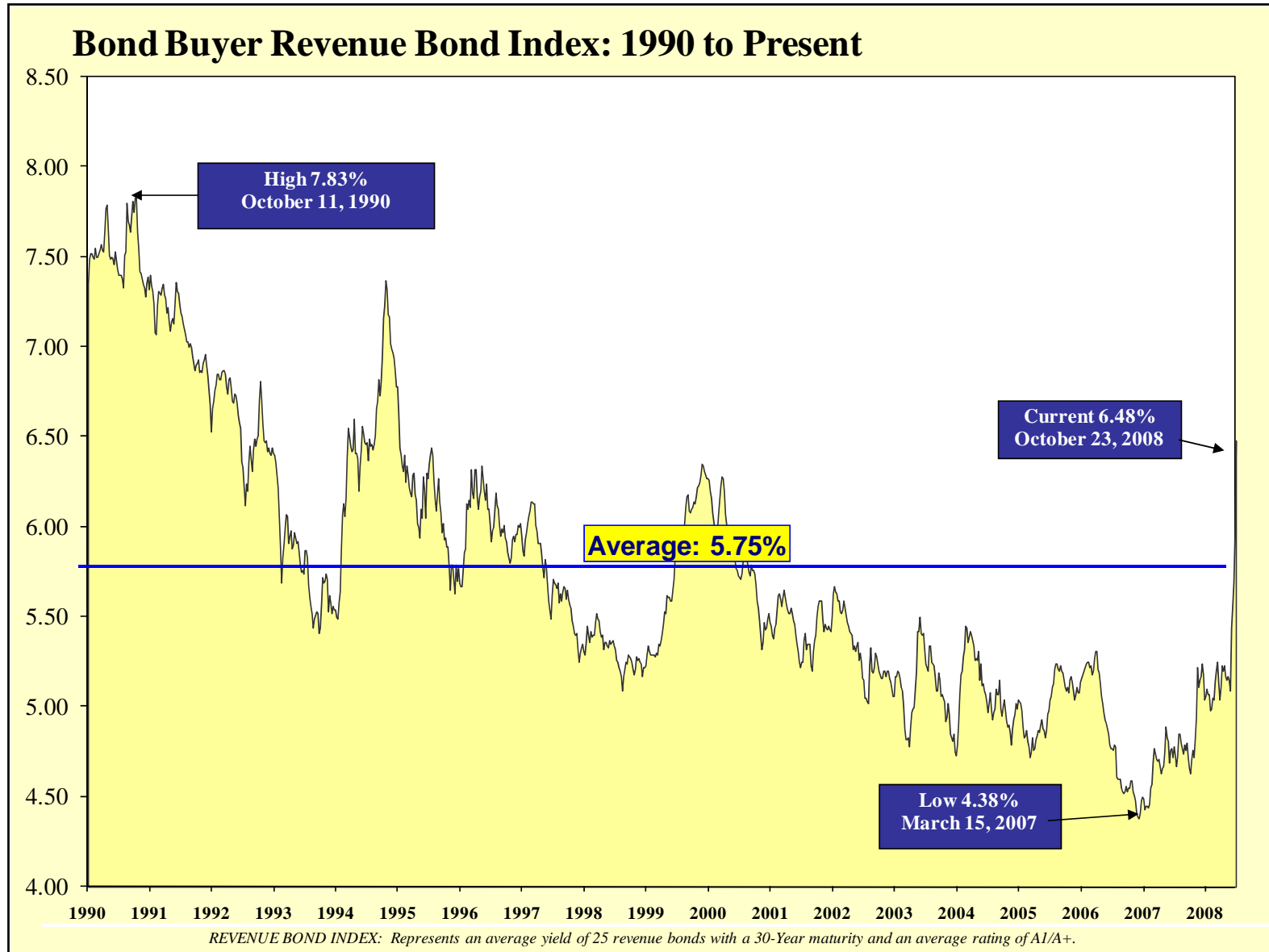
5 Year Historical SIFMA Index



**SIFMA vs. 70% of 1 Month LIBOR: Last 5 Years**







10/23/2007

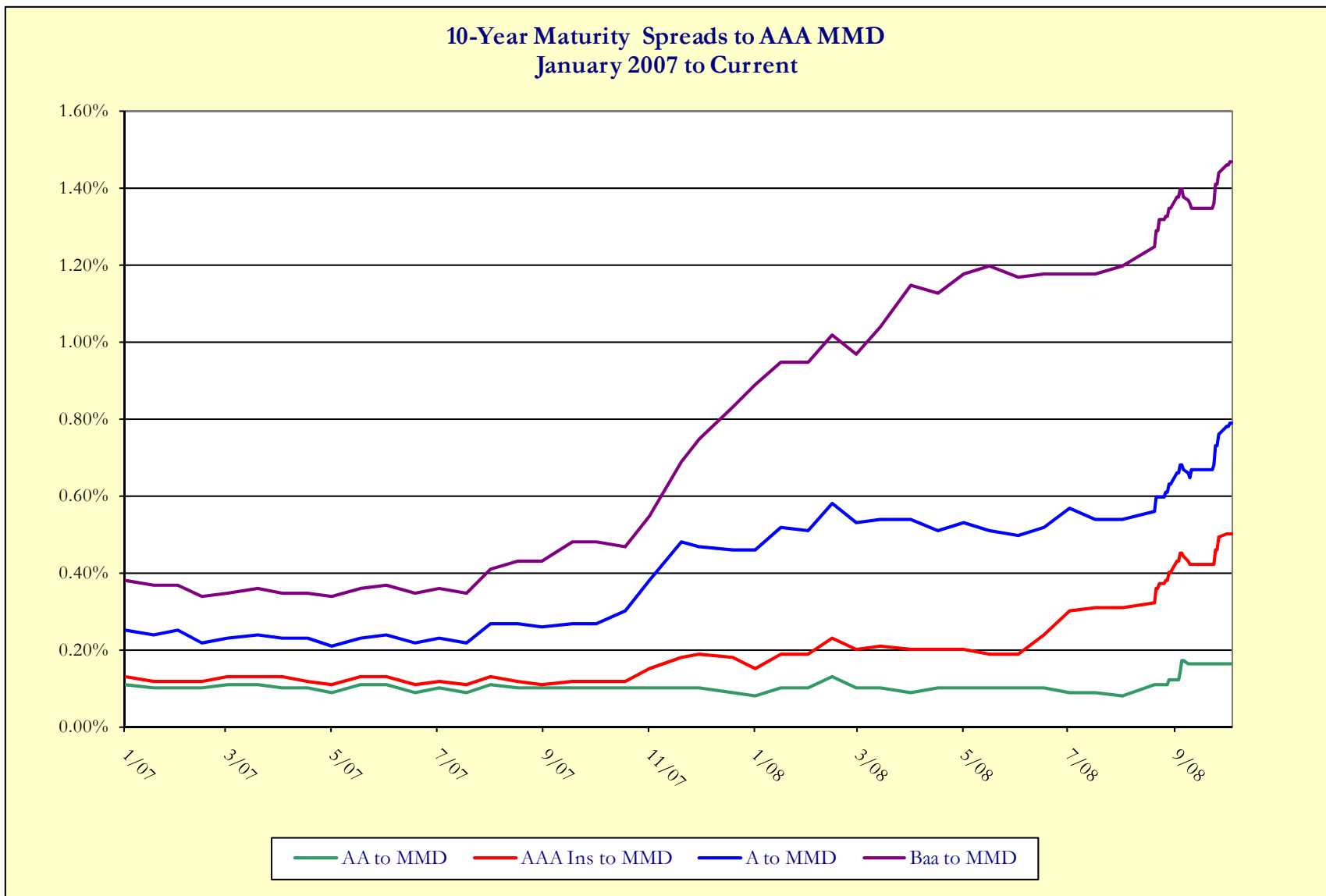
AAA/Baa Spread  
10 Yr. = 49bps  
25Yr. = 53bps

		General Obligations				["AAA" Coupon Range]			
		"AAA"	PRE-RE INSURED	"AA"	"A"	"BAA"	"LOW"	"HIGH"	
1	2008	3.35	3.37	3.38	3.37	3.46	3.65	5.00	
2	2009	3.35	3.40	3.42	3.42	3.53	3.71	5.00	
3	2010	3.37	3.45	3.46	3.45	3.58	3.77	5.00	
4	2011	3.40	3.48	3.50	3.49	3.62	3.82	5.00	
5	2012	3.44	3.52	3.54	3.53	3.67	3.88	5.00	
6	2013	3.72	3.59	3.57	3.73	3.90	4.10	5.00	
7	2014	3.72	3.65	3.63	3.79	3.96	4.16	5.00	
8	2015	3.72	3.70	3.68	3.85	4.03	4.23	5.00	
9	2016	3.62	3.77	3.75	3.93	4.11	4.31	5.00	
10	2017	3.72	3.84	3.82	4.01	4.21	4.41	5.00	
11	2018	3.79	3.91	3.89	4.08	4.29	4.49	5.00	
12	2019	3.84	3.96	3.94	4.14	4.35	4.55	5.00	
13	2020	3.89	4.01	3.99	4.20	4.40	4.60	5.00	
14	2021	3.94	4.06	4.04	4.25	4.45	4.65	5.00	
15	2022	3.98	4.09	4.08	4.29	4.49	4.69	5.00	
16	2023	4.01	4.12	4.11	4.33	4.53	4.73	5.00	
17	2024	4.04	4.15	4.14	4.37	4.56	4.76	5.00	
18	2025	4.07	4.18	4.17	4.40	4.59	4.79	5.00	
19	2026	4.10	4.21	4.20	4.43	4.62	4.82	5.00	
20	2027	4.13	4.24	4.23	4.46	4.65	4.85	5.00	
21	2028	4.16	4.27	4.26	4.49	4.68	4.88	5.00	
22	2029	4.24	4.30	4.29	4.52	4.71	4.91	5.00	
23	2030	4.24	4.32	4.31	4.55	4.74	4.94	5.00	
24	2031	4.25	4.33	4.32	4.57	4.76	4.96	5.00	
25	2032	4.24	4.34	4.33	4.59	4.77	4.97	5.00	
26	2033	4.25	4.35	4.34	4.60	4.78	4.98	5.00	
27	2034	4.26	4.36	4.35	4.61	4.79	4.99	5.00	
28	2035	4.27	4.37	4.36	4.62	4.80	5.00	5.00	
29	2036	4.28	4.38	4.37	4.62	4.80	5.00	5.00	
30	2037	4.28	4.38	4.37	4.62	4.80	5.00	5.00	

10/23/2008

AAA/Baa Spread  
10Yr. = 148bps  
25 Yr. = 140 bps

		General Obligations				["AAA" Coupon Range]			
		"AAA"	PRE-RE INSURED	"AA"	"A"	"BAA"	"LOW"	"HIGH"	
1	2009	1.80	1.80	2.11	1.86	2.38	3.04	5.50	
2	2010	2.73	2.73	3.10	2.83	3.36	4.14	5.50	
3	2011	3.09	3.09	3.55	3.21	3.81	4.60	5.50	
4	2012	3.43	3.43	3.88	3.56	4.16	4.95	5.50	
5	2013	3.63	3.63	4.10	3.76	4.38	5.15	5.50	
6	2014	3.96	4.28	3.96	4.58	5.15	5.50	5.50	
7	2015	4.56	4.47	4.13	4.77	5.50	5.50	5.50	
8	2016	4.56	4.68	4.32	4.96	5.50	5.50	5.50	
9	2017	4.37	4.87	4.51	5.16	5.85	5.50	5.50	
10	2018	4.56	5.06	4.69	5.36	6.04	5.50	5.50	
11	2019	4.71	5.20	4.83	5.52	6.15	5.50	5.50	
12	2020	4.84	5.33	4.96	5.68	6.24	5.50	5.50	
13	2021	4.94	5.42	5.06	5.81	6.34	5.50	5.50	
14	2022	4.99	5.46	5.11	5.87	6.39	5.50	5.50	
15	2023	5.04	5.48	5.16	5.92	6.44	5.50	5.50	
16	2024	5.08	5.50	5.20	5.95	6.48	5.50	5.50	
17	2025	5.12	5.52	5.24	5.98	6.52	5.50	5.50	
18	2026	5.14	5.54	5.26	6.00	6.54	5.50	5.50	
19	2027	5.17	5.56	5.29	6.02	6.57	5.50	5.50	
20	2028	5.21	5.58	5.33	6.05	6.61	5.50	5.50	
21	2029	5.25	5.60	5.37	6.08	6.65	5.50	5.50	
22	2030	5.32	5.62	5.39	6.10	6.69	5.50	5.50	
23	2031	5.35	5.64	5.41	6.12	6.73	5.50	5.50	
24	2032	5.38	5.65	5.43	6.13	6.77	5.50	5.50	
25	2033	5.32	5.66	5.44	6.14	6.72	5.50	5.50	
26	2034	5.33	5.67	5.45	6.15	6.73	5.50	5.50	
27	2035	5.34	5.68	5.46	6.16	6.74	5.50	5.50	
28	2036	5.35	5.69	5.47	6.17	6.75	5.50	5.50	
29	2037	5.36	5.70	5.47	6.18	6.76	5.50	5.50	
30	2038	5.37	5.71	5.48	6.19	6.77	5.50	5.50	



*10-Year and 30-Year MMD vs. Treasury  
(Since January 2007)*



## **Bond Insurer Ratings Grid**

Updated as of 10/20/2008 9:26:25 AM

	RATING ISSUED BY	AMBAC	AGC	CIFG	FGIC	FSA	MBIA	BHAC	Syncora Guarantee	ACA	Radian
<b>Ratings</b>	Moody's	Aa3	Aaa	Ba2	B1	Aaa	A2	Aaa	B2	NA	A3
	S&P	AA	AAA	B	BB	AAA	AA	AAA	BBB-	NA	BBB+
	Fitch	WR	AAA	CCC	CCC	AAA	WR	NR	NR	WR	WR
<b>Outlook</b>	Moody's	Negative	Negative	Negative	Negative	Negative	Negative	Stable	Positive	NA	Negative
	S&P	Negative	Stable	Developing	Negative	Negative	Negative	Stable	Negative	NA	Negative
	Fitch	N/A	Stable	Evolving	Evolving	Stable	N/A	N/A	N/A	N/A	WR
<b>Watch List (UnderReview)</b>	Moody's	Yes	Yes	Yes	Yes	Yes	Yes	N/A	Yes	NA	Yes
	S&P	Yes	No	Yes	Yes	Yes	Yes	No	Yes	NA	No
	Fitch	N/A	No	Yes	Yes	No	N/A	N/A	Yes	NA	WR

Home  
 Market News  
 Regional Spotlight  
 Washington  
 Investors & Investing  
 Underwriters & Dealers  
 Insurers  
 Rating Agencies  
 Market Statistics  
 Last 5 Issues  
 New-Issue Calendar  
 Bond Sales Results

Friday, October 24, 2008

Search the Last Year


[Advanced Search](#)

[Legal Notices](#) | [Web Exclusives](#) | [Special Reports](#) | [Conferences/Events](#) | [Related Sites](#) | [Contact Us](#) | [New Here?](#)

[Manage Your Account](#)

## Credit Crunch Hits Variable-Rate Market

*Fallout from Bond Insurer Downgrades*

Friday, February 29, 2008

By Dakin Campbell

[Print](#) [Email](#) [Reprints](#)

The credit crunch that for weeks has roiled the municipal auction-rate market is now spreading to the market for variable-rate demand bonds, where issuers have sought cover from rising rates.

Much like the dislocation in the auction-rate market, the problems in the variable-rate market can be attributed to questions about ratings of the bond insurers and the constricted availability of Wall Street's capital.

In the last month, the ratings for XL Capital Assurance Inc. and Financial Guaranty Insurance Co. have been knocked down to the A-level from triple-A by the rating agencies, and other bond insurers are being reviewed for downgrades. This has made many money market funds - required to hold at least double-A rated credits under rule 2a-7 - nervous, and led many to shy away from the market or get out of certain floaters.

"The problem that we are having is that under rule 2a-7, as the bond insurers get downgraded, a lot of these bonds are no longer money-market eligible," said Paul Rosenstiel, the deputy treasurer of California.

And so money market funds have shifted the debt to the remarketing agents, like the 2007 top-three of Citi, JPMorgan, and Banc of America Securities LLC, which set the weekly reset rates for variable-rate debt. Faced with the potential of greater supply, the banks can buy up the bonds and take them onto their inventory, or they can direct investors to draw on the liquidity facility.

The banks "wanted to remarket them and the only way you remarket them is taking them in," said one Wall Street trader. "But with the suspect insurance, people put bonds back to the remarketers and they've reached their critical mass."

In increasing numbers, remarketers are directing investors to draw on the liquidity bank that backstops the variable-rate debt. Liquidity is called through a process of investors filing a tender notice to the trustee of their intent to put back the bonds. In some cases, remarketers are directing investors to do that even before attempting to sell the bonds.

"We're getting tenders on almost every bond we have out there every week," said Brian Mayhew, the chief financial officer for the Bay Area Toll Authority. "We haven't had an actual put to a facility yet."

It is this "put" that makes variable-rate demand obligations different than auction-rate securities. Liquidity provided by a letter of credit bank, or a standby purchase agreement provider, gives investors a guaranteed market for the securities if they want to sell them.

Most liquidity banks expect the facility never to be drawn upon, despite a 1982 regulation that said notices should be tendered every week to the trustee and then the bonds sold, Mayhew said. Over the last few decades, remarketing banks bought up any excess supply to support the remarketing,

"What was ordinary and customary would have deemed [hitting the liquidity facility] completely unacceptable," said Michael Marz, vice chair at First Southwest. "In the market we are in now what's ordinary and customary doesn't exist anymore. We are just trying to survive with overwhelming bad news every day."

### RELATED GRAPHIC

[Click to enlarge](#)

### RELATED LINKS

[Insurance Against Insurers](#) - February 27, 2008

[N.Y. Issuers Eye Exit From Auction Market](#) - February 22, 2008

### RELATED TOPICS

[Market Turmoil Hits Munis](#)

Advertisement

## Maximize Your Compliance Tools

- ▶ Private Business Use Monitoring
- ▶ Variable-Rate Reporting
- ▶ Issuer/Conduit Borrower Bidding in ARS Auctions
- ▶ Real-Time Trades
- ▶ Compliance Reporting
- ▶ Record Retention

Most Popular  Emailed  Viewed

Searched

1. [Munis Rally As Demand Roars Back](#)
2. [MIAC Gets N.Y.'s OK To Become Guarantor](#)
3. [N.Y. Official Eyes TARP For Insurers](#)
4. [ARS Still Weighing Down Issuers](#)
5. [San Diego County Rethinks VRDOs](#)
6. [S&P Takes California Off Negative Watch](#)
7. [Former Bear Banker Joins Ramirez](#)
8. [With 'Market on Fire,' Yields Fall 5 Basis Points](#)
9. [Brazos Agency Extends Deadline to Tender Student Loan Debt](#)
10. [GFOA Issues RPs Discouraging FAs From Becoming Underwriters](#)

Advertisement

### UPCOMING EVENTS

[FINRA: Fall Securities Conference](#)

October 22 - 24, 2008  
 Carlsbad, CA

[NFMA Introduction to Municipal Bond Credit Analysis](#)

October 23 - 24, 2008  
 Philadelphia, PA

[TFMA Treasury and Capital Markets Legal & Legislative Issues Conference](#)

Problems began to appear in the variable-rate market in November, when two New York colleges saw rates skyrocket on VRDBs insured by Radian Asset Assurance Inc.

On Wednesday, the Municipal Market Data Variable-Rate Demand Index reset at 3.03%. That is a two-week jump of 214 basis points from the 0.89% rate it was at Feb. 13.

Rising rates and increased capital draws on liquidity providers could pose additional problems for issuers, especially for those looking to get out of auction-rate securities and into variable rate demand bonds. As liquidity banks find themselves facing increasing numbers of puts, they are also trying to deal with an increase in requests for liquidity and letters of credit.

"With the number of auction rates that tried to jump to VRDBs, I think everybody is at capacity," Mayhew said. "There is more capacity, but at a price that you would not want to pay and in terms that are probably unacceptable."

And that capacity seems to be for only the highest-rated credits. The state of Wisconsin, rated AA-minus by both Standard & Poor's and Fitch Ratings, and Aa3 by Moody's Investors Service, has had trouble finding liquidity for a commercial paper program, said Frank Hoadley, Wisconsin capital finance director.

"We've had one party say no and had some unenthusiastic responses from others," Hoadley said.

The state has steered clear of the variable-rate market because of concerns about many of the current issues, but Hoadley said several banks have said they had capital capacity concerns, while others said there would be time constraints in getting the deal done.

And in some cases, banks that have offered liquidity facilities for issuers looking to get out of auction-rate securities and into variable-rate demand obligations are now telling their clients they have to wait.

October 29 - 30, 2008  
Washington, DC

[The Bond Buyer's 14th Annual Midwest Public Finance Conference](#)

November 10 - 11, 2008  
Chicago, IL

[More articles in Underwriters & Dealers](#)

---

[The Bond Buyer Today](#) | [About](#) | [Advertise](#) | [Contact Us](#) | [Customer Service](#) | [Register](#) | [Site Map](#) | [Subscribe](#)

[Privacy Policy](#) | [Subscriber Agreement & Terms of Use](#)

© 2008 The Bond Buyer and SourceMedia Inc., All rights reserved. Use, duplication, or sale of this service, or data contained herein, except as described in the subscription agreement, is strictly prohibited. Trademarks page.

Client Services 1-800-221-1809, 8:30am - 5:30pm, ET

Visit other SourceMedia sites:

Select Site 

- Home
- Market News
- Regional Spotlight
- Washington
- Investors & Investing
- Underwriters & Dealers
- Insurers
- Rating Agencies
- Market Statistics
- Last 5 Issues
- New-Issue Calendar
- Bond Sales Results



Friday, October 24, 2008

Search the Last Year

Go

[Advanced Search](#)



**Check out what's new at The Bond Buyer Online...**

**FREE WEEK** Starts October 27th

- Legal Notices
- Executive Placement
- Manage Your Account
- Web Exclusives
- Special Reports
- Conferences/Events
- Related Sites
- Contact Us
- New Here?

## Bear Deal Shakes Market

*JPMorgan's Move Allays Some Fears*

Tuesday, March 18, 2008

By Dakin Campbell

[Print](#) [Email](#) [Reprints](#)



Click to see a related story in the *American Banker*.

As municipal market participants arrived at work Monday morning, many set to examining the magnitude of JPMorgan's purchase of Bear, Stearns & Co., the fifth largest investment bank in the country.

*Jamie Dimon*

JPMorgan Chase & Co. bought Bear Stearns for \$240 million Sunday, guaranteeing commitments put at risk by margin calls that occurred over the last week. The draw of funds out of Bear Stearns led to many concerns that the bank would not be able to stand behind its commitments in the municipal market, where it serves as a counterparty on billions of dollars in derivative transactions.

Though not the largest, Bear Stearns is one of the "big eight" firms responsible for municipal derivatives, said Peter Shapiro, managing director at Swap Financial Group.

The deal, in which JPMorgan guarantees the trading commitments of Bear Stearns, appears to ease concerns that the troubles of the bank might spread to the governments and municipalities.

"JPMorgan Chase stands behind Bear Stearns," said Jamie Dimon, chief executive officer of JPMorgan Chase. "Bear Stearns' clients and counterparties should feel secure that JPMorgan is guaranteeing Bear Stearns' counterparty risk."

In surveying the news, and gauging the depth and safety of JPMorgan's guarantee, issuers and their advisors turned to the documents and conditions underlying the deals where Bear served as the counterparty. What they found is that in most cases, two subsidiaries are listed as counterparties: Bear Stearns Capital Markets and Bear Stearns Financial Products.

With the assumed completion of the JPMorgan deal - expected to be finalized by the end of the second quarter - the larger bank will serve as the guarantor of last resort. Much like investors asked for additional credit enhancement on bonds backed by downgraded bond insurers, JPMorgan will now serve as an additional guarantee for those subsidiaries, said one source.

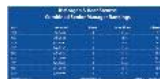
"The way we read it, it looks like a strong guarantee," Shapiro said. "We're still sorting through the fine print."

One concern, Shapiro said, is for those issuers whose exposure to different counterparties is not diversified. If a large percentage of the portfolio is exposed to JPMorgan and Bear Stearns, the resulting portfolio after the transaction is completed will have even greater reliance on JPMorgan.

Market saturation in derivatives is certainly possible as the merged JPMorgan-Bear Stearns company would be the number one underwriter in 2008, serving as senior manager on 52 deals worth a combined \$8 billion through March 16, according to Thomson Financial. Going back to 2000, the merged company would have been second or third most active senior manager every single year.

The nature of each swap agreement depends on what is written into the International Swaps and Derivatives Association swap document language, called the master settlement.

### RELATED GRAPHIC



[Click to enlarge](#)

### RELATED LINKS

[Issuers of Bear-Led Deals Resting Easier After JPMorgan Move - March 18, 2008](#)

### RELATED TOPICS

[Market Turmoil Hits Munis](#)

Advertisement

## Maximize Your Compliance Tools

- ▶ Private Business Use Monitoring
- ▶ Variable-Rate Reporting
- ▶ Issuer/Conduit Borrower Bidding in ARS Auctions
- ▶ Real-Time Trades
- ▶ Compliance Reporting
- ▶ Record Retention

Most Popular  Emailed  Viewed

Searched

1. [Munis Rally As Demand Roars Back](#)
2. [MIAC Gets N.Y.'s OK To Become Guarantor](#)
3. [N.Y. Official Eyes TARP For Insurers](#)
4. [ARS Still Weighing Down Issuers](#)
5. [San Diego County Rethinks VRDOs](#)
6. [S&P Takes California Off Negative Watch](#)
7. [Former Bear Banker Joins Ramirez](#)
8. [With 'Market on Fire,' Yields Fall 5 Basis Points](#)
9. [Brazos Agency Extends Deadline to Tender Student Loan Debt](#)
10. [GFOA Issues RPs Discouraging FAs From Becoming Underwriters](#)

Advertisement



I need lawyers who know that being green takes more than recycling old ideas.

**NIXON PEABODY<sup>LLP</sup>**  
ATTORNEYS AT LAW

### UPCOMING EVENTS

[FINRA: Fall Securities Conference](#)  
October 22 - 24, 2008  
Carlsbad, CA

[NFMA Introduction to Municipal Bond Credit Analysis](#)  
October 23 - 24, 2008  
Philadelphia, PA

[TFMA Treasury and Capital Markets Legal & Legislative Issues Conference](#)

The specific agreements govern whether a concerned issuer can exit a derivative transaction after a deal such as the JPMorgan-Bear transaction.

"Every transaction is different," said Linda D'Onofrio, partner at Blank Rome LLP.

Under ISDA regulations, there are standard events of default and termination events included in the documents. Within those, the parties can make changes or ensure that certain ones do not apply. A number of provisions also relate to mergers and acquisitions, and of those, three main conditions apply where an issuer can terminate the swap.

One of these is a termination event called a "credit event upon merger." In this case, a buying firm takes over the selling firms' assets. An issuer can terminate this transaction if the newly created firm is materially weaker from a credit standpoint than the original firm tied to the swap. The terms of this provision appear to most closely resemble the recent JPMorgan transaction, but the conditions do not because of JPMorgan's relative strength to that of Bear Stearns prior to the transaction.

"Traditionally Bear Stearns in the last several years has been among the lower rated among the top underwriters," said Peter Block, managing director with Standard & Poor's.

On Friday, all three rating agencies downgraded the corporate rating of Bear Stearns, and Monday Fitch Ratings updated the rating to reflect the beneficial effects of JPMorgan's involvement, moving Bear's rating to A-minus, from BBB. The rating remains on watch positive. Standard & Poor's moved the Bear rating to watch with developing implications, while Moody's Investors Service placed the rating on review for upgrade. All three affirmed JPMorgan's rating at AA-minus, AA-minus, and Aa2, respectively.

The second condition relates to an event of default called a "merger without assumption." This happens only in the case when the credit event upon merger does not occur, when the stronger entity fails to take responsibility for the assets and obligations of the weaker firm. The default occurs only as long as the credit support document - in which some transactions pledge the credit of a separate entity - does not apply.

And the third condition in which an issuer can terminate a swap related to a merged company under ISDA rules is through additional credit events, negotiated by the two parties before agreeing signing the contract. This could be tied to the ratings of the counterparty or any other event to which the two parties agree.

Many of these conditions depend on the deal's final structure, and many market participants agreed in saying that it was early in the process and difficult to predict the exact nature of the deal.

In the meantime, JPMorgan will guarantee the existing contracts, as well as all those completed between now and the date the purchase is completed or canceled. The Federal Reserve has already given its approval, and the sale is now subject to the approval of shareholders.

And while shareholders may be reluctant to approve the sale because it values the shares at such a deep discount - \$2 a share when the stock traded near \$30 on Friday - they may not have a choice. Many analysts have suggested that if JPMorgan had not agreed to the deal, Bear Stearns would be forced into bankruptcy.

Senate Banking Committee chairman Christopher Dodd, D-Conn., seemed to agree when he told reporters yesterday during a conference call that the federal government and JPMorgan took the "right action over the weekend" because "the alternative was a filing of bankruptcy by Bear Stearns."

With months to go before the final approvals are secured and the deal finalized, Shapiro advised issuers to keep a close watch as the details of the merger take shape.

"The major concern we have is if Bear shareholders turn down the merger," Shapiro said.

Lynn Hume, Ted Phillips, and Caitlin Devitt contributed to this story.

October 29 - 30, 2008  
Washington, DC

[The Bond Buyer's 14th Annual Midwest Public Finance Conference](#)  
November 10 - 11, 2008  
Chicago, IL

[The Bond Buyer Today](#) | [About](#) | [Advertise](#) | [Contact Us](#) | [Customer Service](#) | [Register](#) | [Site Map](#) | [Subscribe](#)

[Privacy Policy](#) | [Subscriber Agreement & Terms of Use](#)

© 2008 The Bond Buyer and SourceMedia Inc., All rights reserved. Use, duplication, or sale of this service, or data contained herein, except as described in the subscription agreement, is strictly prohibited. Trademarks page.

Client Services 1-800-221-1809, 8:30am - 5:30pm, ET

Visit other SourceMedia sites:

Select Site 