Policy Details

I. Purposes for Use of Derivatives
   A. Reduce exposure to changes in interest rates on a particular or anticipated future financial transaction.
   B. Lower net cost of borrowing.
   C. Achieve higher rate of return on investment.
   D. Manage variable rate exposure on debt issuance.
   E. Manage the risk of future cash inflows and outflows.
   F. Reduce exposure to changes in foreign currency prices.
   G. Reduce exposure to fluctuations in price for commodity purchases.
   H. Achieve a better matching of assets and liabilities.

II. Principles Governing Use of Derivatives
   A. Derivatives are to be used for hedging purposes and not for speculation.
   B. Derivatives may be used to better manage assets and liabilities and to lower overall costs and reduce interest rate risk.
   C. Derivatives must be documented using agreements that contain terms and conditions as set forth in the International Swaps and Derivatives Association (ISDA) Master Agreement, as modified by an appropriate ISDA schedule, confirmation, and/or credit support annex. This requirement shall not apply to standardized exchange-traded products such as futures contracts executed through a trading exchange.
   D. Counterparties to any derivative agreement must have a long-term credit rating of A or above by a nationally recognized rating agency if the swap is uncollateralized. Counterparties with a lower rating will be required to post collateral.
University Policy

Applies to: All university personnel responsible for the management of university debt and financial assets excluding the Office of Investments.

E. A swap dealer may be deemed to be acting as an advisor to the university under certain circumstances with respect to a specific swap or trading strategy involving a swap. The university may engage a third party, or use a university employee, to serve as a qualified independent representative to provide independent advice and oversight of any swap or trading strategy involving a swap, in which case the swap dealer will not be deemed to be acting as an advisor to the university.

F. Derivative agreements should not require the university to post collateral unless approved by the vice president for financial services and treasurer or the senior vice president for business and finance and chief financial officer.

III. Risks Associated with Derivatives
   A. Counterparty risk – the risk of a failure by a counterparty to perform as required under the agreement.
   B. Termination risk – the ability of either party to terminate the agreement prior to maturity. Early termination could result in adverse results.
   C. Amortization risk – the risk that the cashflow schedule of the derivative does not exactly match the cash flow schedule of the asset/liability. This can result in a less than satisfactory hedge and create unnecessary risk.
   D. Basis risk – arises as a result of movements in interest rates that may not be in tandem between the asset/liability and the derivative instrument. This could create a favorable or unfavorable cost differential.
   E. Tax risk – the risk that tax laws may change resulting in an unexpected movement in the value of the hedge.
   F. Liquidity risk – the risk that collateral is not posted when due resulting in possible exposure to loss.
   G. Regulatory risk – the risk that laws and regulations may change resulting in unexpected movement in the value of the hedge and/or additional compliance requirements.
   H. Compliance risk – not complying with laws and regulations can result in penalties, fines or the inability to do additional transactions.

PROCEDURE

Issued: 06/07/2013
Reviewed: 01/01/2015

I. Approval and Oversight
   A. The vice president for financial services and treasurer in collaboration with the senior vice president of business and finance and chief financial officer shall make the determination if any derivative transaction is in the best interests of the university.
   B. All derivative agreements shall receive prior approval of the chair of the Finance Committee of the Board of Trustees. All completed derivative transactions will be reported to the chair of the Finance Committee of the Board of Trustees within five business days of execution.
   C. All derivative agreements must be reviewed and approved by legal counsel prior to execution.
   D. Derivative agreements may be executed only by the vice president for financial services and treasurer or the senior vice president of business and finance and chief financial officer.
   E. Derivative agreements may be terminated before maturity upon approval of the senior vice president of business and finance and chief financial officer.
   F. The vice president for financial services and treasurer or the senior vice president of business and finance and chief financial officer will determine whether to engage a third party or use a university employee to serve as a qualified independent representative regarding a specific derivative or trading strategy involving a derivative. In the event the determination is made to engage a third party, the applicable agreement may be executed only by the vice president for financial services and treasurer or the senior vice president of business and finance and chief financial officer.
G. The Office of Financial Services is responsible for oversight, monitoring and compliance with applicable rules and regulations for any derivative transaction.

Responsibilities

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<th>Position or Office</th>
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| Vice president for financial services and treasurer     | 1. Collaborate with the senior vice president of business and finance and chief financial officer to determine if any derivative transaction is in the best interests of the university.  
2. Execute derivative agreements as appropriate.  
3. Determine whether to engage a third party or use a university employee to serve as a qualified independent representative regarding a specific derivative or trading strategy involving a derivative.  
4. Execute applicable agreement with third party engaged to serve as a qualified independent representative regarding a specific derivative or trading strategy involving a derivative. |
| Senior vice president of business and finance and chief financial officer | 1. Collaborate with the vice president for financial services and treasurer to determine if any derivative transaction is in the best interests of the university.  
2. Execute derivative agreements as appropriate.  
3. Terminate derivative agreements before maturity as appropriate.  
4. Determine whether to engage a third party or use a university employee to serve as a qualified independent representative regarding a specific derivative or trading strategy involving a derivative.  
5. Execute applicable agreement with third party engaged to serve as a qualified independent representative regarding a specific derivative or trading strategy involving a derivative. |
| Chair of the Finance Committee of the Board of Trustees | 1. Review and approve all derivative agreements prior to execution.  
2. Receive reports on all completed derivative transactions within five business days of execution. |
| Qualified independent representative                    | Provide an independent evaluation of the transaction and risk, including fair pricing and appropriateness of the transaction. |
| Office of Financial Services                             | Oversee, monitor, and ensure compliance with applicable rules and regulations for any derivative transaction. |
| Office of Legal Affairs                                  | Review and approve all derivative agreements prior to execution. |

Resources

Contacts

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<th>Subject</th>
<th>Office</th>
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| Policy questions      | Office of Financial Services    | 614-292-6261  
800-678-6009  
Fax: 614-292-7568 | www.treasurer.ohio-state.edu/ |

History

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