

Operational Procedures

LOCAL CURRENCY HEDGES WITH THE IDB



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1. INTRODUCTION

1.1. Purpose

- 1.1.1 The IDB offers borrowers the option to request and execute local currency swaps with the Inter-American Development Bank (the Bank) to hedge currency exposures with the Bank, with the limitation that such swaps cannot exceed existing outstanding loan balances (OLBs).¹
- 1.1.2 The purpose of this document is to set out the operational procedures for requesting and executing such local currency swaps (the LC Swap Transactions, as defined in paragraph 1.5 below) between the Bank and a borrower (the Borrower) in one or multiple loans granted by the Bank.
- 1.1.3 LC Swaps with borrowers require the signing of an International Swap Dealers Association Master Agreement (ISDA), which provides the general conditions under which a Borrower contracts local currency swaps with the Bank. Unlike market practice between commercial entities, the Bank does not require a Credit Support Annex (CSA) or the posting of collateral for sovereign guaranteed transactions.² However, the ISDA Schedule and the Loan Agreements include cross-default provisions; i.e., arrears on the loans can trigger an early termination of the LC Swap Transaction and payment delays on LC Swap Transactions can trigger arrears sanctions on the loans.

1.2. Applicability

- 1.2.1. These Operational Procedures apply to all LC Swap Transactions requested by a Borrower. The Bank may modify these Operational Procedures from time to time. Any such modifications will apply only to LC Swap Transactions requested after the date of such modifications and will not affect any outstanding LC Swap Transactions, or/and LC Swap Transactions requested, but not yet executed, prior to the date of any such modification. The latest version of these Operational Procedures is available on the Bank's website at www.iadb.org/flexiblefinancing. Borrowers that have signed ISDAs with the Bank will be notified of any amendments to these Operational Procedures. In the event of any inconsistency between these Operational Procedures and the ISDA or the Confirmation under the ISDA (the Confirmation), the ISDA or the Confirmation shall prevail.

1.3. Definitions

The terms below have the designated meanings wherever used in these Operational Procedures:

- a. "Calculation Agent" means the Bank in relation to LC Swap Transactions between the Bank and the Borrower. All determinations made by such Calculation Agent will be final, conclusive and obligatory for the parties (except in the case of obvious error), and will be duly documented, in good faith, and in a commercially reasonable manner.

¹ With the implementation of the FFF, Borrowers also have the ability to request and execute any IDB borrowing and non-borrowing member country currency swaps with the Bank. Please contact us to discuss this and other hedging options with the Bank.

² This provision may change should new regulations were to impact the manner in which IDB conducts its hedging operations.

- b. “Execution Period” is the period during which the Bank can execute its Market Transaction in connection with a LC Swap Transaction as specified in the LC Swap Request Letter. The Execution Period starts from the date the LC Swap Request Letter is received by the Bank and will end a specified number of calendar days later, as specified in the LC Swap Request Letter.
- c. “Market Counterparty” means a party with which the Bank enters into a derivatives transaction in the financial markets.
- d. “Market Transaction” means a local currency swap transaction entered into by the Bank with a Market Counterparty in connection with a LC Swap Transaction with a Borrower.
- e. “Screen Rate” means a market rate displayed by established information vendors such as, but not limited to, Bloomberg or Reuters.
- f. “LC Swap Transaction” is a cross-currency swap between the Bank and the Borrower in which the Borrower pays periodically a stream of future cash flow amounts in the currency of its own country, and receives periodically in exchange from the Bank a stream of future cash flow amounts in a convertible currency from the inception of the transaction until its termination.
- g. “Request Letter” is an irrevocable request from the Borrower to the Bank to execute a LC Swap Transaction under the terms specified in the Request Letter. A sample of a Request Letter is provided in Annex A.³
- h. “Units of Account” means the financial unit used as a means of expressing the obligations of Borrowers to pay principal and interest outstanding on loans granted under the Bank’s Currency Pool System.

³ The Bank may modify the sample Request Letter from time to time.

1.4. Eligibility

- 1.4.1. LC Swap Transactions are offered against OLBs of one or multiple loans with the same Borrower with the limitation that the sum of outstanding notional amounts of the LC Swap Transactions' convertible currency legs must be less than the underlying OLB in the same convertible currency during the life of the transaction.
- 1.4.2. Currencies that can be swapped into local currency include all currencies in which the Bank offers loans; i.e., USD, CHF, EUR and JPY, as long as the Borrower has an OLB with the Bank in such currency. For this purpose, outstanding balances in Units of Accounts of the Currency Pool System (CPS) loans are currently comprised as 50% USD, 25% JPY, 12.5% EUR, and 12.5% CHF⁴.
- 1.4.3. On the convertible currency leg of the LC Swap Transaction, the Borrower can receive a floating or fixed interest rate at a level the Borrower designates, consistent with the interest rate paid by the Borrower on the underlying OLB.
- 1.4.4. On the local currency leg of the LC Swap Transaction, the Borrower pays the local currency interest rate equivalent to the interest rate chosen on the receivable leg. This interest rate reflects market conditions prevailing when the Bank executed its Market Transactions. The Borrower can choose to pay the local currency (LC) equivalent rate in a fixed, floating or inflation-indexed interest rate type, subject to market availability.

1.5. Documentation

- 1.5.1. International Swaps and Derivatives Association (ISDA) Master Agreement: Swap Transactions will be documented under an ISDA Master Agreement to be entered into between the Bank and a Borrower. For each LC Swap Transaction entered into between the Bank and a Borrower, a Confirmation will be executed. A sample of a Confirmation is provided in Annex B⁵.
- 1.5.2. Amendments to Loan and Guarantee Agreements: Before a LC Swap Transaction can be requested under an ISDA, an amendment letter will need to be executed amending, to the extent practicable, all Loan and Guarantee Agreements between the Borrower and the Bank to establish the necessary provision(s) for cross default between the LC Swap Transactions executed under the ISDA and the Loan Agreement(s).

2. REQUEST FOR A LC SWAP TRANSACTION

2.1. General

- 2.1.1. A Borrower may at any time submit a request for a LC Swap Transaction to the Bank. The Bank will only consider a Request Letter made substantially in the form specified in Annex A. Such Request Letter is binding and irrevocable as per its terms and conditions.

⁴ Currencies' percentage compositions in the CPS may change over time.

⁵ Confirmations will be prepared for each operation executed, on a case by case basis, and may differ from the model provided in this Operational Procedures.

- 2.1.2. In the Request Letter, a Borrower must specify the desired terms of the LC Swap Transaction including the effective date, the convertible currency amount, the fixed interest rate or spread over LIBOR, and the maximum fixed interest rate or spread in LC the Borrower is willing to pay under such LC Swap Transaction. All terms will only be effected at the prevailing market foreign exchange rate.
- 2.1.3. Given the volatility of interest and foreign exchange rates, the Bank gives no assurance that it will be able to obtain the rate specified in the Request Letter, even if such an interest rate were to prevail at any given point during the Execution Period. If, during the Execution Period, the Bank is unable to execute the LC Swap Transaction on the terms requested by the Borrower, the Request Letter will expire, and the Bank will promptly notify the Borrower thereof. After the Execution Period has expired, the Borrower may send the Bank a new Request Letter, which can have different terms and conditions.
- 2.1.4. Unless the Bank otherwise agrees, the minimum notional amount of a LC Swap Transaction in a single Request Letter is US\$10,000,000 equivalent.
- 2.1.5. The maximum amount of a LC Swap Transaction that a Borrower may specify in a single Request Letter will be subject to market availability during the Execution Period. The Bank may, at the request of the Borrower, provide information about the amount that could be executed. The information provided by the Bank is not binding and does not commit the Bank to execute that amount, or any other amount available, during the Execution Period.

2.2. **Communication of Request Letter**

- 2.2.1. Each Request Letter, duly signed, will be furnished to the Bank at the email address and facsimile number specified below and will be deemed received by the Bank: (a) on the date it is received by the Bank at the email addresses specified below; and (b) on the date received in legible form by the Bank at the facsimile numbers specified below:

Claudia Franco, Head Client Services	cfranco@iadb.org
Finance Loan Portfolio Services	FIN-FSV-LPS@iadb.org
IDB Country Office Representative	

2.3. **Authorized Representative and Address of Borrower for Purposes of Making Requests**

The representative from the Borrower designated in the ISDA is authorized to sign Request Letters. The Borrower's address for the purpose of these Operational Procedures is the address specified in the ISDA. The representative of the Borrower may, by written notice and in a manner that is satisfactory to the Bank at the address specified in the ISDA, authorize additional persons to sign Request Letters. Before, or at the time the Request Letter is submitted, written authorization of any additional person to sign the Request Letters, and the specimen signature of such authorized person, must be supplied to the Bank together with his/her title and address, including telephone and fax numbers, as well as email address.

3. EXECUTION

3.1. General

- 3.1.1. The Bank will exercise reasonable efforts to execute any Request Letter, which is in form and substance satisfactory to the Bank within the Execution Period established in the Request Letter. However, the Bank will not be liable if, in the exercise of such reasonable efforts, it fails to do so.
- 3.1.2. In executing a LC Swap Transaction, the Bank will exercise the same standard of care as it uses with respect to transactions it enters into in accordance with its fiduciary responsibilities. Since interest and exchange rates may fluctuate throughout the Execution Period, and the range of rates will only be known after the end of the Execution Period, the Bank cannot ensure the resulting financial terms it will obtain in executing the LC Swap Transaction.
- 3.1.3. Borrowers should note that the availability of LC Swap Transactions depends on the existence of a liquid swap market in the currency being requested.
- 3.1.4. If, during the Execution Period, any national or international calamity or development, crisis of a political or economic nature, or change in the financial markets in which a LC Swap Transaction may be executed has occurred, the effect of which, in the judgment of the Bank, would materially and adversely affect its ability to execute such LC Swap Transaction, the Bank will notify the Borrower of such circumstances, and the Bank and the Borrower together will determine what actions, if any, should be taken with respect to the Request Letter.

3.2. Review of Request Letter

Upon receipt of a Request Letter, the Bank will review it to determine whether the information presented meets the requirements specified in these Operational Procedures.

3.3. Non-complying Requests; Re-submission

If the Bank determines that a Request Letter does not comply with the requirements specified in these Operational Procedures, the Bank will, within the Execution Period, notify the Borrower that such Request Letter fails to meet certain requirements and cannot be executed. In that case, the Bank will take no further action to execute the LC Swap Transaction. The Borrower may re-submit a Request Letter complying with the requirements. Such Request Letter will be treated as a new Request Letter for the purposes of calculating the Execution Period.

4. TRANSACTION FEES

4.1. Transactions for Which a Fee is Payable

The Borrower will pay to the Bank a transaction fee on the notional amount of any LC Swap Transaction.

4.2. **Amount of fee payable**

The fees charged by the Bank in respect to LC Swap Transactions can be found at www.iadb.org/rates. Transaction fees charged by the Bank may be revised from time to time and the revised fees will apply to LC Swap Transactions effected after such revisions.

4.3. **Currency of Payment of Transaction Fees Transaction fees will be payable as follows:**

Transaction fees will be payable on a per annum basis on the notional amount in the LC leg of the swap and included in the LC Swap Transaction.

5. MARKET QUOTES DISRUPTION EVENTS

The parties acknowledge that a LC Swap Transaction is entered into in connection with the Bank's corresponding Market Transaction. The parties therefore agree that, notwithstanding the occurrence of any disruption event that may materially affect the currency exchange rates, and/or interest rate and inflation adjustments applicable to payments of the LC Swap Transactions, the Borrower's payment obligations shall remain consistent with the terms of the corresponding Market Transaction. To ensure such consistency, the parties expressly agree that the Bank, in its role as Calculation Agent, will in good faith and in a commercially reasonable manner, make every effort to reflect the corresponding source of funding of the Bank, and shall determine (a) the existence of such disruption event(s) and (b) the applicable interest rate or fallback rate to determine the appropriate amount(s) to be paid by the Borrower.

6. VOLUNTARY EARLY TERMINATION OF LC SWAP TRANSACTIONS THE BANK WILL ROUND ALL CURRENCY

- 6.1. In addition to the events of default and termination events contemplated in the ISDA, the parties may agree to terminate a LC Swap Transaction on terms acceptable to the Bank before its maturity provided that the Bank is able to unwind its Market Transaction and that other operational considerations related to such unwinding are satisfactorily resolved. Any gain or loss that the Bank incurs as part of this unwinding (i.e., the market value of the swap at that time) will be passed on to the Borrower.
- 6.2. To terminate a LC Swap Transaction before its maturity as provided in Section 6.1, either partially or in its entirety, the Borrower shall submit an irrevocable early termination request (the "Early Termination Request") to the Bank at least thirty (30) calendar days prior to the proposed early termination date. The Borrower shall specify an early termination date that should coincide with one of the interest or principal payment dates specified in the schedule established in the Confirmation. The Borrower shall also specify the amount(s) and transaction(s) it requests to be terminated before maturity. The minimum amount for which the Borrower may request the early termination of an LC Swap Transaction is five million dollars (US\$5,000,000), unless the existing balance of a LC Swap Transaction is less than such amount.
- 6.3. If the Early Termination Request is acceptable and the Bank is able to satisfactorily unwind its Market Transaction, as established above, the Bank will proceed to terminate the LC Swap Transaction as soon as practicable and will subsequently notify the Borrower.

7. DELAY IN PAYMENTS UNDER LC SWAP TRANSACTIONS

- 7.1. The Borrower's failure to pay, when due, any payment under a LC Swap Transaction, if such failure is not remedied on or before the third local business day after notice of such failure is given to the Borrower, shall constitute an event of default, and the Bank shall have the right to terminate all outstanding LC Swap Transactions. Additionally, the Bank will not enter into any new LC Swap Transactions with the Borrower if any Bank loan is overdue by 30 calendar days or more.
- 7.2. If termination of the LC Swap Transactions results in a net amount payable from the Bank to the Borrower, such amount will be applied against overdue amounts. If the termination of the Swap Transaction results in an amount payable by the Borrower to the Bank, such amount will be immediately due and payable to the Bank.

ANNEXES

Annex A MODEL OF REQUEST LETTER FOR LOCAL CURRENCY SWAP TRANSACTIONS

(Counterparty letterhead)

Date: [Date]

To: Inter-American Development Bank

Attention: [Name of official]

The purpose of this letter is to request a swap transaction under the ISDA Master Agreement dated as of ____ between the Inter-American Development Bank (IADB) and the [Counterparty]. The desired terms and conditions of the requested swap transaction are as follows:

GENERAL TERMS

Effective Date:	[mm/dd/yyyy]
Termination Date:	[mm/dd/yyyy]
Execution Period:	[mm/dd/yyyy to mm/dd/yyyy]

CONVERTIBLE CURRENCY PAYER

Convertible Currency:	[USD][EUR][JPY][CHF]
Convertible Currency Interest Rate Payer:	IADB
Convertible Currency Notional Amount:	[] [See Attached Schedule]
Convertible Currency Payment Dates:	[dd/mm] [dd/mm] each year from the Effective Date until the Termination Date.
<u>Convertible Currency Interest Rate Type:</u>	<u>Options (1) or (2):</u> (1) Fixed Interest Rate; (2) Spread over LIBOR.

Option (1) – Fixed Interest Rate

Convertible Currency Fixed Interest Rate:	[x %]
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Convertible Currency Day Count Fraction: [30/360] [Act/360] [other]

Option (2) – Spread Over LIBOR

Convertible Currency Spread: [x basis points]
Designated Maturity: [3 months][6 months][other]
Reset Dates: []
Convertible Currency Day Count Fraction: [30/360] [Act/360] [other]
Compounding: [Applicable [with][without] spread][Not Applicable]

LOCAL CURRENCY PAYER

Local Currency: [COP]
Local Currency Payer: [Counterparty]
Local Currency Payment Frequency: [annual] [semiannual] [other]
Local Currency Payment Dates: [dd/mm] [dd/mm] each year from the Effective Date until the Termination Date.
Local Currency Interest Rate Type: Options (1), (2) or (3):
(1) Fixed Interest Rate;
(2) Spread Over Floating Rate Index;
(3) Fixed Interest Rate on a Notional Adjusted by Inflation.

Option (1) – Fixed Interest Rate

Maximum Local Currency Fixed Interest Rate: [x %]
Local Currency Day Count Fraction: [30/360] [Act/360] [other]

Option (2) – Spread Over Floating Rate Index

Maximum Local Currency Spread: [x basis points]
Local Currency Floating Rate Index: [IPC] [DTF] [Other]
Designated Maturity: [3 months][6 months][other]
Local Currency Day Count Fraction: [30/360] [Act/360] [other]
Reset Dates: []
Compounding: [Applicable [with][without] spread][Not Applicable]

Option (3) – Fixed Interest Rate on a Notional Adjusted by Inflation

Maximum Local Currency Fixed Interest Rate: [x %]
Local Currency Inflation Index: [UVR] [other]
Notional Adjustment Formula: []
Local Currency Day Count Fraction: [30/360] [Act/360] [other]

This request is irrevocable and the [Counterparty] acknowledges that IADB provides no assurance that it will be able to fulfill the request, even if the terms described above were to prevail in the market at any given time during the Execution Period specified herein. If IADB fulfills the request, [Counterparty] agrees to sign a Confirmation including the terms provided herein, and incorporating the applicable terms and conditions of the above-referenced ISDA Master Agreement, which shall be submitted to [the Counterparty] for signature and shall be signed and returned to IADB by [the Counterparty].

Sincerely,

[the Counterparty]

[Name]

[Title]

Annex B MODEL OF LOCAL CURRENCY SWAP TRANSACTION ISDA CONFIRMATION

Date: [Date]

To: [Counterparty]

Attention: [Name of official]

Telefax No.: [Number]

From: Inter American Development Bank
10th Floor, Stop [.]
1300 New York Avenue, NW,
Washington, DC 20577

Telefax No.: 202-623-[.]

Transaction Reference Number: [TBD]

The purpose of this letter agreement is to confirm the terms and conditions of the Transaction entered into between:

INTER AMERICAN DEVELOPMENT BANK (“IADB”)

and

[COUNTERPARTY] (THE “COUNTERPARTY”)

on the Trade Date specified below and identified by the Reference Number specified below (the “Transaction”) and evidences a complete and binding agreement between us as to the terms of the Transaction. This letter agreement constitutes a “Confirmation” as referred to in the ISDA Master Agreement specified below.

The definitions and provisions contained in the 2000 ISDA Definitions (the “Swap Definitions”), as published by the International Swaps and Derivatives Association, Inc. (“ISDA”) are incorporated into this Confirmation. Capitalized terms shall have the definitions provided therein.

1. This Confirmation supplements, forms a part of and is subject to the ISDA Master Agreement dated as of [TBD] between IADB and the Counterparty (the agreement, as amended and supplemented from time to time, being referred to herein as the “Master Agreement”). All provisions contained in, or incorporated by reference to, the Master Agreement shall govern the Transaction referenced in this Confirmation except as expressly modified herein. In the event of any inconsistency between this Confirmation and the Definitions or Master Agreement, this Confirmation shall prevail.

2. The terms of the particular Transaction to which this Confirmation relates are as follows:

General Terms:

Trade Date:	[]
Effective Date:	[]
Termination Date:	[]
Calculation Agent:	IADB
Governing Law:	New York law

Local Currency Amounts:

Local Currency:	[]
Local Currency Payer Notional Amount:	[]
Local Currency Payer:	Counterparty
Local Currency Calculation Period End Dates:	[]
Local Currency Payment Dates:	[]
Business Days:	[]
Local Currency Payer Interest Rate:	[]
Local Currency Payment Amounts:	[]
Local Currency Day Count Fraction:	[]
Settlement of Local Currency Payment Amounts:	[]
Local Currency Reset Date:	[]
Local Currency Floating Rate Index:	[]
Floating Rate:	[]
Local Currency Spread:	[]
Compounding:	[]

Convertible Currency Amounts:

Convertible Currency	[USD][EUR][JPY][CHF]
Convertible Currency [Floating][Fixed] Rate Payer:	IADB
Convertible Currency Calculation Period End Dates:	[]
Business Days Applicable to Convertible Currency Calculation Period End Dates:	[]
Convertible Currency Payment Dates:	[]
Business Days Applicable to Convertible Currency Payment Dates:	[]
Convertible Currency Notional Amount:	[]
Convertible Currency [Floating Rate Option][Fixed Rate]:	[]
Convertible Currency Spread:	[]
Designated Maturity:	[]
Reset Dates:	[]
Convertible Currency Day Count Fraction:	[]
Compounding:	[]
Convertible Currency Amounts:	[]

Initial Exchange:

Initial Exchange Date:	The Effective Date
IADB Initial Exchange Amount:	Local Currency Notional Amount
Counterparty Initial Exchange Amount:	Convertible Currency Notional Amount

Interim Exchanges:

Local Currency Payer Interim Exchange Amounts:	[]
Convertible Currency Payer Interim Exchange Amounts:	[]

Final Exchange:

Final Exchange Date:	The Termination Date
IADB Final Exchange Amount:	Convertible Currency Notional Amount
Counterparty Final Exchange Amount:	Local Currency Notional Amount

Fee Payable to IADB:

Amount of Fee Payable to IADB:	[0.25%] of Convertible Currency Notional Amount
Currency of Payment:	Convertible Currency
Payment Date:	[TBD]

Terms Relating to Settlement Currency:

	(This section is included in case the settlement currency is a convertible currency)
Settlement Currency:	Convertible Currency
Reference Currency:	Local Currency
Settlement Foreign Exchange Rate:	[]
Valuation Date:	[]
Business Day Applicable to the Valuation Date:	[]

3. Additional Provisions

Each party represents to the other party that (absent a written agreement between the parties that expressly imposes affirmative obligations to the contrary for this Transaction):

(a) *Non-Reliance.* It is acting on its own account, and it has made its own independent decisions to enter into this Transaction and as to whether this Transaction is appropriate or proper for it based upon its own judgment and upon advice from such advisers as it has deemed necessary. It is not relying on any communication (written or oral) of the other party as investment advice or as a recommendation to enter into this Transaction; it being understood that information and explanations related to the terms and conditions of this Transaction shall not be considered investment advice or a recommendation to enter into this Transaction. No communication (written or oral) received from the other party shall be deemed to be an assurance or guarantee as to the expected results of this Transaction.

(b) *Assessment and Understanding.* It is capable of assessing the merits of and understanding (on its own behalf or through independent professional advice), and understands and accepts, the terms, conditions and risks of this Transaction. It is capable of assuming, and assumes the risks of this Transaction.

(c) *Status of Parties.* The other party is not acting as a fiduciary for or an adviser to it in respect of this Transaction.

4. Offices:

For purposes of this Transaction, IADB is acting through its [TBD] Office.

For purposes of this Transaction, Counterparty is acting through its [TBD] Office

5. Account Details

Payments to IADB:

Account for payments in Convertible Currency:

Favour:	[TBD]
[ABA/Bank No.:[Swift BICCODE:]]	[TBD]
Account No.:	[TBD]
Reference:	[TBD]

Account for payments in Local Currency:

Favour:	[TBD]
[ABA/Bank No.:[Swift BICCODE:]]	[TBD]
Account No.:	[TBD]
Reference:	[TBD]

Payments to Counterparty:

Account for payments in Convertible Currency:

Favour:	[TBD]
[ABA/Bank No.:][Swift BICCODE:]	[TBD]
Account No.:	[TBD]
Reference:	[TBD]

Account for payments in Convertible Currency:

Favour:	[TBD]
[ABA/Bank No.:][Swift BICCODE:]	[TBD]
Account No.:	[TBD]
Reference:	[TBD]

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing a copy of this Confirmation and returning it to us or by sending to us a letter, Swift or facsimile substantially similar to this letter, which letter, swift or facsimile sets forth the material terms of the Transaction to which this Confirmation relates and indicates agreement to those terms. When referring to this Confirmation, please indicate: IADB Reference Number(s): [TBD]

Yours sincerely,

For and on behalf of IADB

By: _____
Authorized Signature Name:
 Title:

Confirmed as of the date first above written:

For and on behalf of [COUNTERPARTY]

By: _____
Authorized Signature Name:
 Title: