Public Financing Advisory Committee

Special Meeting and Study Session

Thursday, January 4, 2017 at 1:30 pm

Hall of Administration Planning Commission Room

MEETING MINUTES

Attendees: Shari Freidenrich (Committee Member), Carl Groner (Committee Member), Thomas Hammond (Committee Member), John J. Moohr (Committee Member), Wallace Rodecker (Vice Chair), Eric Woolery (Committee Member), Lisa Hughes (Chair) Frank Kim, (County Executive Officer), Suzanne Luster (Public Finance Director), Angie Daftary (County Counsel), Ronnie Magsaysay (County Counsel), Michelle Aguirre (Chief Financial Officer), Steve Delaney (Orange County Employees Retirement System Chief Executive Officer).

I. **Call to Order/Introductions/Opening Remarks:** Meeting called to order by Chairwoman Lisa Hughes at 1:32 pm. Member Rodecker suggested moving the election of 2017 Chair and Vice Chair to after the study session and the committee agreed.

II. **Review and Approval of Minutes:** Meeting Minutes of December 8, 2016 were approved with an amendment. Member Rodecker moved the minutes, Member Moohr seconded. The amended minutes passed unanimously.

III. **Study Session:** Treasurer Freidenrich is recused and left the dais due to a conflicting interest, if approved, the Treasurer will be purchasing the private placement pension obligation bonds from the County. Chair Hughes distributed the Third Amended and Restated County of Orange Policies and Procedures for PFAC (PFAC policy).

Chair Hughes read from the PFAC policy Item 1. "Assure that all public financings involving the County of Orange are in compliance with all applicable state and federal laws."; Item III from page 4 "No public financing the proceeds of which shall be used primarily for the purpose of investment for arbitrage shall be approved by the Committee." These are policies the committee needs to follow. Ms. Luster explained the purpose for issuing the bonds was to receive a prepayment discount that has occurred every consecutive year since January 2011.

Discussion continued on the 2015 OCERS investment loss of $9 million, reflected on the comparison spreadsheet provided by Public Finance which purpose was to reflect prepaying vs. not prepaying and benefits of the program. The gross prepayment discount for the 2015 POB was estimated at $21 million with a 5.8% prepayment discount. Also, 2011 had a loss of approximately $4.2 million. The remaining years since 2011 reflected positive returns.

Chair Hughes asked how the 2015 loss of $9 million was absorbed. Ms. Luster explained the market loss or gain is applied to the unfunded liability. Mr. Delaney, Orange County Employees Retirement System (OCERS) Chief Executive Officer explained that OCERS guarantees a discount but whether or not we earn the amount is not guaranteed. Mr. Kim explained that we do the pension prepayment in order to receive the 4.5% discount, absent a pension prepayment we are still making contributions to OCERS over 26 pay periods a year and our expectation is to earn 7.25%, the actuarial assumed rate of return. Whether we do the financing or not, we expect money transferred to be invested and earning the assumption of 4.5% for the prepayment and 7.25% if paid over 26 pay periods. If the rate is not achieved the difference is included in the overall asset value as part of the annual calculation and valuations included in the forthcoming rates in the following year.

There was a discussion regarding the bonds being issued for arbitrage. Ms. Luster explained the County issues these pension bonds for the purpose of receiving a budget savings for the upcoming year and not issued for arbitrage.

Mr. Delaney provided a presentation with Paul Angelo, Actuary from Segal, on the phone. The main points were the prepayment program is a management tool for plan sponsors. It is a tool offered by statute through the legislature. OCERS Board has broad authority under the constitution to offer programs that benefit the plan and plan sponsors.

Chair Hughes read Government Code 315.82 sub-section B, “make an advance payment of all or part of the County’s estimated annual contribution to the retirement fund provided that the payment is made within 30 days after the commencement of the County’s fiscal year.” There is a problem with issuance of the Pension Obligation Bonds because the payment needs to be made within 30 days. She indicated that she spoke to Former County Treasurer, now Senator Moorlach regarding this issue. Chair Hughes stated he would be happy to carry emergency legislation in order to fix this problem. Chair Hughes added that even though there is a default judgment which had no opposition there is still a problem. The County requested that future obligations would come under this validation proceeding.

Phil Morgan, Bond Counsel from Orrick, explained that they read that statute differently because that statute doesn’t address the situation of the prepayment in advance of the fiscal year which was pointed out to the court. The court rendered a default judgment through the validation statutes. The court was aware of this statute. Additional bonds were authorized in the Board of Supervisors original resolution. The court’s view as once authorized the bonds are in existence for the validation process. The court found all agreements are legal, valid, and binding, and the time to challenge was within 30 days. Chair Hughes stated there is a problem with issuance of future bonds. She disagrees that the court made a finding that the code section does not limit it. Mr. Morgan read section 870a of the Code of Civil Procedure. There continued to be discussion on the validation proceeding and issuance of additional bonds.

Mr. Kim stated that in regards to this code section he has been given consistent and clear advice by both County Counsel and Bond Counsel that this is a valid financing and this is who is relied upon.

Member Woolery stated that his main argument was the growing pension liability. Most recently this legal issue has been presented questioning the statute within “30 days” of the fiscal year end. What does that mean to Mr. Morgan?

Mr. Morgan replied that he believes that statue was addressing the situation of prepayment of normal annual contribution for the then current fiscal year. Mr. Morgan does not believe it is addressing the early prepayment and secondly, this was in front of the court and entered a default judgment without appeal. Mr. Morgan stated that there is a paragraph in the trust agreement that more or less says even if there are no bonds outstanding this trust agreement will remain in existence for purposes of its validation and being able to issue additional bonds. Additional bonds can be issued under the trust agreement and continue to apply within the documentation represented to the Board.

Mr. Kim clarified rates are established by OCERS. There is a cost obligation over the next 18 months whether we issue the debt or not. This is a cash flow financings which could be paid from reserves. Mr. Kim also clarified that the County could make the payment 18 months in advance and get a discount or make it over 26 pay periods. We are not guaranteed a rate of return. OCERS has an assumption of a revenue stream from each of their sponsors and they invest monies in accordance with their investment policy to achieve their stated return investment assumption. Whether the payment is made over 26 pay periods or one payment the risk remains. Risk is factored into the discount rate.

Mr. Kim stated he will reach out to Senator Moorlach and make available our bond attorneys to discuss this issue.

Member Rodecker informed the committee of his issues with this item which included; 1) Loss of money in 2015 which was one of the best economies in a long time 2) Why are proceeds not going to the pension fund 3) This seems like arbitrage in which we are not allowed to do and violating one of our own rules 4) The legal issue that Senator Moorlach is willing to address before voting 5) Default judgment of 2007 only addresses some of our concerns, have other problems such as the 30 days. There are a lot of problems before we can say it is great.

Mr. Moohr has concerns regarding the losses. Ms. Luster referred to the document titled "OCERS Rate of Return" which was previously provided and pointed out to Member Moohr that 19 out of the last 30 years the actual rate of return exceeded the assumed rate of return which was 7.25% or previously higher at 7.75%.

It is explained that each year OCERS votes and offers the discount, then it is included the County Strategic Financial Plan (SFP) process and it is taken to the Board in December. Because OCERS has offered the discount and the County has participated in the past, it is programmed into the Strategic Financial Plan and may be approved by the Board.

Mr. Kim added that the difference between the SFP and an approved Budget is that the SFP is simply a planning tool that is made with assumptions and is a modeling tool to help give a picture of what we can anticipate, none of the things discussed at this meeting have been incorporated into the budget, budget instructions have not even been distributed to departments.

Member Woolery made the following motion 1) We will never support any long-term POBs 2) A long-term strategy to pay down the unfunded pension liability, an actuarial study should be made a) This strategy needs be part of the Strategic Financial Plan b) The strategy makes sure that all federal and state grants are paying their share of the unfunded pension liability c) POBs should be a form of bridge financing to get us to the plan which should be addressed within the next three years d) PFAC needs to get the actual results of previous years POBs as part of the consideration of any future POBs. There is an investment risk associated with the POBs that is associated with the market timing of the bonds and when funds are invested.

An amended motion was made to strike the word "never" and replace it with "not". Member Hammond seconds and the voting went as follows: Member Groner "yes", Member Hammond "yes", Member Moohr "no", Vice Chair Rodecker "no", Member Woolery "yes", Chair Hughes "no", resulting in a tie vote.

Member Rodecker made a motion to add the following language "subject to the Board of Supervisor's overriding the arbitrage restriction if applicable." Member Moohr seconds and voting went as followed: Member Groner "no", Member Hammond "yes", Member Moohr "yes", Vice Chair Rodecker "yes", Member Woolery "yes", Chair Hughes "no". Motion passed.

IV. **Election of the Public Financing Advisory Committee 2017 Chair and Vice Chair:** The committee decided to defer this item until the next meeting.

V. **Public Comments:** None

VI. **Committee Comments:** None

VII. **Date of next meeting**: January 12, 2017 at 1:30 pm

VIII. **Adjournment:** This meeting was adjourned at 3:51 pm