County of Los Angeles
CHIEF EXECUTIVE OFFICE
Kenneth Hahn Hall of Administration
500 West Temple Street, Room 713, Los Angeles, California 90012
(213) 974-1101
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WILLIAM T FUJIOKA
Chief Executive Officer

ADOPTED
BOARD OF SUPERVISORS
COUNTY OF LOS ANGELES

13 SEPTEMBER 15, 2009

Sachi A. Hamai
SACHI A. HAMAI
EXECUTIVE OFFICER

September 16, 2009

The Honorable Board of Supervisors
County of Los Angeles
383 Kenneth Hahn Hall of Administration
500 West Temple Street
Los Angeles, CA 90012

Dear Supervisors:

LOS ANGELES COUNTY CONDUIT FINANCING POLICY
WITHDRAWAL FROM MEMBERSHIP IN THE
CALIFORNIA STATEWIDE COMMUNITIES DEVELOPMENT AUTHORITY
(ALL DISTRICTS) (3 VOTES)

IT IS RECOMMENDED THAT YOUR BOARD:

Authorize the Chief Executive Officer to take all necessary actions for the County to withdraw its membership from the California Statewide Communities Development Authority (CSCDA), a joint powers authority (JPA) established for the purpose of issuing bonds and engaging in conduit financing activities.

PURPOSE AND JUSTIFICATION OF RECOMMENDED ACTION

On May 27, 2008, my Office provided your Board with a policy recommendation to govern the County's participation in conduit financings (attached). It was determined that going forward the County would not become a member of any new or additional conduit financing JPA and that the County should withdraw from CSCDA, the only such JPA of which we are currently a member.

The County's withdrawal from CSCDA will have no negative impact on the financing operations of the County and will not prevent worthwhile projects from having access to tax-exempt bond financing. The recommendation in this Board letter represents the final step in the development of the County's new conduit financing policy.

After the County's participation in the recently approved tax-exempt financing for Southern California Presbyterian Homes is completed, we request your approval to formally terminate the County's membership in the Joint Exercise of Powers Agreement with CSCDA.

Implementation of Strategic Plan Goals

This action supports the County's Strategic Plan Goal #1 - Operational Effectiveness: Strategy #1 – Fiscal Sustainability through the implementation of a conduit financing policy that minimizes the risk exposure to the County resulting from conduit financing transactions.

FISCAL IMPACT

There will be no fiscal impact to the County budget.

BACKGROUND AND LEGAL REQUIREMENTS

On May 27, 2008, my Office recommended the following policies with respect to the County's participation in conduit financings:

- The County will not become a member of any new or existing conduit financing JPA and will terminate its membership with CSCDA. Currently, CSCDA is the only conduit financing entity in which the County is a member.

- The Treasurer and Tax Collector will process all conduit financing requests in Los Angeles County, provided that any project located within an incorporated city is supported by the City Council or applicable Councilmember. In each case the County or one of its affiliated authorities can serve as the bond issuer.

- No borrower will be required to use a JPA such as CSCDA or its competitors to serve as bond issuer. However, if a borrower chooses to pursue a financing in an incorporated city through a JPA, any request for "elected official" approval of the financing will be referred to the appropriate municipal government.

- If a conduit financing project includes multiple facilities in different counties, the borrower will be referred to the appropriate State financing authority for assistance. State authorities have statewide jurisdiction and the "elected official" approval is provided by the Governor.

All of the above procedures are intended to protect the County from potential liability, as well as to further your Board's public policy goals. Compliance with the new conduit financing policy will help ensure that bond proceeds are spent as originally intended and that the County's residents will in fact derive the expected public benefits.

The process of providing tax-exempt financing to private entities is referred to as "conduit" financing because the issuer serves as a conduit between the public capital markets (as lender) and the private (usually non-profit) borrower. For all projects located within its boundaries, the County (acting through the Treasurer and Tax Collector) may elect to serve as the conduit issuer for qualified private borrowers. The bonds so issued would be payable solely from funds of the private borrower and the bondholders would have no recourse to County revenues or assets.

In 1988, the California State Association of Counties and the League of California Cities jointly sponsored the creation of CSCDA to serve as a conduit financing bond issuer throughout the State of California (the County became a member of CSCDA in 1997). Unlike a financing authority administered directly by the County or the State, CSCDA is a shell entity operated solely by a private contractor. Similar to other private conduit issuers, CSCDA is not subject to the same reporting and oversight rules that apply to the County and the State. This relative lack of public scrutiny, transparency and regulation is a concern given that CSCDA now ranks as one of the ten largest (of more than 3,000 total) issuers of tax-exempt debt nationwide.

In accordance with Section 13 (Withdrawal and Addition of Parties) of the Amended and Restated Joint Exercise of Powers Agreement Relating to the California Statewide Communities Development Authority (the "Agreement"), the County may withdraw from the Agreement upon written notice to CSCDA. The withdrawal shall be effective following CSCDA's written acknowledgement of this notice and the subsequent filing of such notice as an amendment to the Agreement. It is our intention to transmit the withdrawal notice to CSCDA immediately following your Board's approval of this recommendation and the completion of the County's participation in the Southern California Presbyterian Homes bond issuance.

IMPACT ON CURRENT SERVICES (OR PROJECTS)

None to the County. Private borrowers within Los Angeles County will retain access to tax-exempt financing through the policies outlined above.

CONCLUSION

Upon approval of the recommendation to withdraw from CSCDA, please return two executed copies of the adopted Board Letter.

Respectfully submitted,

WILLIAM T FUJIOKA
Chief Executive Officer

WTF:EFS:ef

Attachment

c: Chef Executive Officer
Acting County Counsel
Executive Officer, Board of Supervisors
Treasurer and Tax Collector

attachment

County of Los Angeles
CHIEF EXECUTIVE OFFICE

713 KENNETH HAHN HALL OF ADMINISTRATION
LOS ANGELES, CALIFORNIA 90012
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WILLIAM T FUJIOKA
Chief Executive Officer

May 27, 2008

To: Supervisor Yvonne B. Burke, Chair
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

From: William T Fujioka
Chief Executive Officer

CONDUIT FINANCING POLICY

On September 20, 2007, in response to a motion by Supervisor Burke and amended by Supervisor Antonovich, this office provided your Board with a report and recommendation (Attachment A) with respect to potential Los Angeles County (County) participation in the Statewide Community Infrastructure Program (SCIP), which is a program sponsored by the California Statewide Communities Development Authority (CSCDA). At that time we indicated that we would return to your Board with this more comprehensive report and policy with respect to County facilitation of conduit financing transactions.

We met with the Treasurer and Tax Collector to discuss conduit financing with CSCDA or CMFA (California Municipal Finance Authority) as compared to existing County-controlled financing entities or statewide authorities administered by the California State Treasurer. We understand that borrowers may prefer dealing with a CMFA or CSCDA-type of organization due to less stringent credit enhancement requirements or the ability to have one agency handle a series of projects done throughout the state. However, from a risk management perspective, we believe it is in the County's best interest to work with borrowers through existing County and State financing entities, which will give the County more protection in a conduit financing transaction.

Recommendations

Going forward, we recommend handling conduit financing requests as set forth below:

The County should not become a member of CMFA or any other conduit Joint Powers Authority (JPA), and the County should terminate its membership in CSCDA. This should not adversely affect any financing projects in Los Angeles County because the borrowers have alternative access to tax-exempt financing as discussed below.

The Treasurer and Tax Collector should process all requests to finance facilities in Los Angeles County, provided that any facility to be financed within an incorporated city is supported by the City Council or applicable Councilmember. In each case the County or one of its affiliated authorities can serve as the bond issuer, regardless of whether the facilities to be financed are located in the unincorporated area or an incorporated city.

No borrower would be required to use a JPA such as CSCDA or CMFA to serve as bond issuer. However, if a borrower chooses to pursue financing for facilities in an incorporated city through a JPA, any request for "elected official" approval of the bonds should be referred to the applicable City.

If multiple facilities in different counties are proposed to be financed, the borrower should be referred to the appropriate State financing authority for assistance. State authorities have statewide jurisdiction and the "elected official" approval is provided by the Governor.

We are currently processing one transaction involving CSCDA, a financing JPA of which the County is presently a member. Upon resolution of that transaction we will file an agenda item with your Board to withdraw from membership in CSCDA.

Background

For more than 20 years, the County has provided tax-exempt financing to private entities for projects and programs that your Board has determined will serve public purposes. Such projects and programs are designed to meet the social needs of the County's residents in the areas of health, public safety, employment, housing and education, and to meet the needs of disabled or aged persons.

The process of providing tax-exempt financing to private entities is referred to as "conduit" financing, because the County serves as a "conduit" between the public capital markets (as lender) and the private (usually non-profit) borrower. A typical conduit financing transaction involves the issuance of bonds by the County (acting through the office of the Treasurer and Tax Collector) or a County-controlled entity[1], with a loan of

[1] County-controlled entities that could serve as issuer in conduit financing transactions include the Los Angeles County Industrial Development Authority, the Los Angeles County Community Development Commission, the Los Angeles County Housing Authority, and the Los Angeles County Public Works Financing Authority.

the bond proceeds to the private borrower. The bonds so issued are payable from loan payments or other revenues received from the private borrower. The bondholders have no recourse to County revenues or assets. In addition, existing County policy requires that the bonds be further secured by a letter of credit, bond insurance, or some other type of credit enhancement.

The County's jurisdiction as a conduit bond issuer extends to all of Los Angeles County. We have financed projects within incorporated cities with the consent of the City Council (or applicable Councilmember in the City of Los Angeles). Borrowers who seek to finance multiple projects throughout the State of California can typically obtain financing through one of six financing authorities with statewide jurisdiction created under State law and administered either through the office of the California State Treasurer or the Governor.[2]

Joint Powers Authorities

In 1988, the California State Association of Counties and the League of California Cities jointly sponsored the creation of CSCDA to serve as a conduit financing bond issuer throughout the State of California. The County became a member of CSCDA in 1997.

More recently, CMFA was created to engage in conduit financing activities that are virtually identical to CSCDA's. The County is not a member of CMFA.

Unlike the financing authorities administered by the County and the State, CSCDA and CMFA are shell entities administered by private contractors. They are not subject to the same reporting and oversight rules that apply to the County and the State Treasurer, nor are they required to provide public notice of meetings at least 10 days in advance, as the State authorities do. This relative lack of public scrutiny, transparency and regulation has caused the State Controller to pursue stronger reporting requirements for JPAs. On February 6, 2008, the Senate Local Government Committee held a hearing to explore questions and concerns about the financing activities of these agencies.

Under State law, a JPA may only finance facilities located within the territorial jurisdiction of its members. As a result, in order for CSCDA or CMFA to finance facilities within the unincorporated area of Los Angeles, the County is required to

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[2] California Alternative Energy and Advanced Transportation Financing Authority, California Educational Facilities Authority, California Pollution Control Financing Authority, California School Finance Authority, California Health Facilities Financing Authority, and California Infrastructure and Economic Development Bank.

become a member of the issuing JPA. Also, under federal law any conduit financing must be approved by an elected official having jurisdiction over the project area. Because CSCDA and CMFA are not governed by elected officials, your Board is often asked to approve their bonds issued to finance projects in Los Angeles County.

Existing Conduit Financing Policy

For your reference, a copy of the County's existing conduit financing policy is attached to this report (Attachment B). These policies have been in place for more than ten years. Of particular note are the following:

1. Requests for financing through "non-state" JPAs (such as CSCDA or CMFA) in incorporated areas will be referred to the appropriate city for necessary TEFRA hearings and "elected official" approval.

The County has recently been asked to approve CMFA bond issues to benefit facilities located in incorporated cities, contrary to existing policy

2. The County will not approve a financing through a "non-state" JPA (such as CSCDA or CMFA) in the unincorporated area, unless the borrower obtains credit enhancement. In addition, all profits from the operation of the facility receiving conduit financing must be used within the boundaries of Los Angeles County for Board-approved programs.

The County has recently been asked to approve CMFA bond issues to benefit facilities located in unincorporated areas without credit enhancement and without dedicating profits to support Board-approved programs, contrary to existing policy.

All of the County conduit financing policies and procedures are intended to protect the County and your Board from potential liability, as well as to further your Board's public policy goals. Compliance with existing policies assures requisite public benefit; controls fees paid by the borrower; allows the County to select or approve the professionals involved in the transaction; and gives the County ongoing monitoring and audit control, helping to ensure that bond proceeds are spent as originally intended so that the County's residents will in fact derive the expected public benefits.

Recent Developments

Issuance volume shifts to JPAs. In the last few years, an increasing number of conduit borrowers have sought financing through CSCDA and CMFA, rather than more traditional issuers such as the County or the State, despite the fact that both CSCDA and CMFA charge one-time and ongoing fees that the County does not charge. The migration of transactions to CSCDA and CMFA is largely the result of their outreach and marketing efforts directed toward non-profit and for-profit borrowers. It also appears to be motivated by the borrowers' belief that the JPAs will close their transactions faster than can the County or the State.

It may be true that the process of obtaining financing through the County can take longer than through CSCDA or CMFA, but this can be explained (at least in part) by the County's more rigorous lending standards and public notice requirements. For example, the JPAs often do not require credit enhancement, and their boards' agendas are not subject to the same reviews and advance filing requirements as your Board's agendas.

Securities law concerns. In the last five years there has also been an evolution in securities litigation, with a trend in Congress and the federal courts toward extending potential liability against third parties who participate in failed bond issues but do not make statements directly to bondholders. This trend increases the risk that the County could become involved in litigation or a work-out situation simply by having approved an issuance of bonds by CMFA or CSCDA if the borrower is unable to meet its debt service obligations.

The increased risk of County involvement in litigation following a borrower's default makes the County's policy requiring credit enhancement all the more important. If the borrower cannot meet its debt service obligations, the credit enhancer will step in and pay off the bondholders, so that the borrower (or the County) can pursue resolution of the default privately with a single institutional creditor rather than a committee of bondholders. In light of the heightened risk, the County should also obtain an opinion of disclosure counsel with respect to the accuracy and adequacy of statements made to investors. Such opinions are always required when the County is the bond issuer, but have not typically been furnished when the issuer is a conduit JPA.

Please contact Ellen Sandt, Deputy Chief Executive Officer of Operations at (213) 974-1186 or Mark Saladino, Treasurer and Tax Collector at (213) 974-2101 if you have any questions.

WTF:ES

Attachments

c: Treasurer and Tax Collector