

1994 Orange County Bankruptcy Issues

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Orange County Bankruptcy

December 6, 1994

- ❑ Investment Driven Failure
- ❑ Losses at \$1.6B
- ❑ Broad gamble on declining interest rates. Rates continued to rise.
- ❑ Deposits of \$7.6 billion, 20.6 billion in investments based on leverage
- ❑ Early December 1st Boston sells \$2 billion of the securities it held as collateral
- ❑ December 6 – Bankruptcy Filing

Orange County Bankruptcy (cont'd.)

Causes:

- ❑ Treasurer not subject to significant formal oversight by board/others
- ❑ Investment securities were unusual, not clearly articulated, leverage unregulated
- ❑ County reporting not well-regulated
- ❑ Yield pressures

Orange County Bankruptcy (cont'd.)

Fallout

- ❑ State Auditor's
Report/recommendations
- ❑ SEC action against County
- ❑ Bankruptcy itself

Legislative Response to Orange County Bankruptcy

- ❑ 1994 (SB1804; 1995 SB866)
- ❑ Treasurer duties/qualifications
- ❑ Limits on investment/leverage
- ❑ Increased oversight/reporting

Oversight

- ❑ Statement of Investment Policy annually, to be considered by legislative body
- ❑ Policy to include type and permitted concentration of investments
- ❑ Quarterly report of investments to legislative body and others with detail on investment and compliance with policy and statement of ability to meet policy expenditure requirement for next 6 months

Treasurer Duties/Oversight

- ❑ County Treasurer investment duties defined – prudent investor standard
 - Safety, liquidity, yield
- ❑ Oversight Committee Created
 - Expertise of members
 - Broad representation of stakeholders
 - Special conflict of interest provisions
 - Duties include annual audit to determine Treasurer compliance with investment policy

Investment Restrictions

- ❑ Ban on inverse floaters, range notes, mortgage derived interest-only strips, any security that could result in zero interest if held to maturity
- ❑ Repurchase Agreements/Reverse Repurchase TRANs proceeds may not be invested for term longer than Note maturity

CASES FOR DISCUSSION

- ❑ Executive Life Insurance Company (1990-1991)
- ❑ Lehman Brothers (September 14-15, 2008)
- ❑ Bond Reserve Fund GICs