
Can Changes to Federal Regulation Help Municipal Finance?

California Debt & Investment Advisory Commission
Bond Buyer Pre-Conference

*“The California Municipal Securities Market in 2009:
Recovery or Requiem?”*

Julia H. Cooper
Deputy Director of Finance
City of San Jose
September 15, 2008

Good Disclosure – What is it? Why Do It? and Who Really Cares?

- Primary Disclosure
 - Development of the Official Statement
 - Providing Financing Team with documents and tools to prepare primary disclosure
- Secondary Market Disclosure
 - Annual Report pursuant to requirements of Continuing Disclosure Agreement/Certificate
 - Comprehensive Annual Financial Report
 - Material Event Notices

Primary Disclosure -- Official Statement

- SEC has made it very clear – ***issuer is primarily liable for contents of its official statement***
 - *“In authorizing the issuance of securities and related disclosure documents, a public official may not authorize disclosure that the official knows to be false; nor may a public official authorize disclosure while recklessly disregarding facts that indicate there is a risk that the disclosure may be misleading”*
- Disclose ***all*** material facts
 - Rule 10b-5 Anti-fraud provisions
 - ***Do not omit*** or ***misstate*** any material fact
- What is material?
 - Important fact to investor in making a decision to purchase the bonds

Secondary Market Disclosure – Key Points

- Preparation of Annual Report, Comprehensive Annual Financial Report, Material Event Notices
- Same standard of care as in preparation of primary market disclosure
- Considerations for Discussion
 - Who prepares and files – centralization generally better
 - Ensure consistency in information disseminated
 - Designate Key City contact for disclosure decisions
 - What makes an event material?
 - Who are the core members of your “disclosure team”?

San Jose Experience – Educational Process

- Active education and dialogue with City Council on matters related to disclosure and financial matters – recent training session during Council meeting
- Audited Financial Statements presented to City Council within 5 months after end of Fiscal Year (year)
 - Since FY 2001-02 Statements of Principal Financial Officer and City Manager included in CAFR

Statement Under Oath of Principal Financial Officer Regarding Facts and Circumstances Relating to the Comprehensive Annual Financial Report (CAFR) For the Fiscal Year Ended June 30, 2006

I, Scott P. Johnson, Director of Finance, state and attest that:

(1) To the best of my actual knowledge and belief, based upon a review of the covered reports of the City of San Jose, and, except as corrected or supplemented in a subsequent covered report:

- The covered report is accurate in all material respects; and
- Is reported in a manner designed to present fairly the financial position and results of operations of the City; and
- No covered report contained an untrue statement of a material fact as of the end of the period covered by such report; and
- No covered report omitted to state a material fact necessary to make the statements in the covered report, in light of the circumstances under which they were made, not misleading as of the end of the period covered by such report.

(2) Each year, upon completion of the City's annual audit of its Financial Statements, City staff, along with the City's external Certified Public Accountant (CPA) auditing firm, present the City's Financial Statements and related independent auditor's report thereon to the Making Government Work Better (MGWB) Committee which then reports out to the full City Council. I will review the contents of this statement with the City Council's MGWB Committee, which functions as the Council's audit committee, at a regularly noticed meeting of the Committee in October of 2006.

(3) In this statement under oath, each of the following, as filed with the City Clerk, is a "covered report":

- The 90th Comprehensive Annual Financial Report of the City of San Jose for the fiscal year ended June 30, 2006;

Any amendments to the foregoing.


Scott P. Johnson
Director of Finance

State of California, County of Santa Clara

On 10/6/06 before me, Mark J. Brogan, Sr., Notary Public, Personally appeared Scott P. Johnson, personally known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that he executed the same in his authorized capacity, and that by his signature on the instrument the person, or the entity upon behalf of which the person acted, executed the instrument.

WITNESS my hand and official seal.


Mark J. Brogan, Sr., Notary Public



San Jose Experience – Evolving Process

- Appendix A – General City Information prepared and updated by City staff – [you own the document](#)
- Actively engage more members of City staff in primary disclosure process
 - Budget Office
 - Retirement
 - Public Works
- Hire separate Disclosure Counsel

San Jose Experience – Constant Challenges

- How do we ensure the right people in the room?
- Are we disclosing enough or too much?
- How do we get other City staff engaged in the conversation?
- How do we avoid/minimize “*Disclosure Creep*”?

San Jose Experience – Evolving Process

- Gather relevant documents and provide to all members of the financing team
- Engage in attorney-client conversations
- Think beyond the financing schedule
 - What documents or information are scheduled to be released, for example Budget and Planning
 - Keep entire financing team apprised of the status of new or emerging information

Good Disclosure – What is it? Why Do It? and Who Really Cares?

- **What is it?**

- Primary – Official Statement
- Secondary – Annual Report

- **Why Do it?**

- Disclosure necessary to access capital market
- Ensures continued access to the capital market

- **Who Really Cares?**

- Apparently a lot of people –
- Federal regulators, Congress, market analysts

SEC Chairman Cox's Recent Comments

Should Issuers be Worried?

- SEC plans to propose as early as end of September rules that would enhance municipal disclosure
- The Bond Buyer reported on September 9, “Cox said ... *turmoil in the municipal market during the past year, in particular the auction-rate securities scandals ... has only served to increase the urgency of his initiatives. He predicted that lawmakers will support them, while tacitly acknowledging that they had been slow to do so up until now*”
- Cox states, ***“A great deal has happened in the markets in the past year, ... If any more evidence were needed that this affects markets in a serious way and touches millions of real investors, events have certainly provided them.”***

SEC Chairman Cox's Recent Comments

Should Issuers be Worried?

- The Bond Buyer article goes on to quote Chairman Cox on the issue ARCs and Jefferson County, AL problems as illustrations of two ***“nearly endemic problems” in municipal finance: “It is simultaneously the case that unsuitable investments might be pushed on to municipal issuers and that municipal issuers have failed to place responsibility for multibillion-dollar financings in the hands of professionally expert, technically competent people.”***
- But Mr. Cox adds, the Tower Amendment *“stands athwart”* of the SEC's efforts to address a range of issues because the commission's direct authority extends only to broker-dealers. The SEC can only ***“pick up the pieces when it's too late for investors,” ... Change is desperately needed there.”***

Yep ... Issuers should be worried

- The Bond Buyer headline on September 15, “*Discord on Disclosure – Cox Comments Sparks Spat on Standards*”
- The Bond Buyer reports, “*State officials warned that such enhancements are not needed and dismissed the idea of that any ongoing market problems ... warrant wholesale changes to the existing municipal market regime.*”
- Public sector colleagues from around the country voiced their objections to Chairman Cox’s comments

Yep ... Issuers should be worried

- Ben Watkins, Director of Florida's Division of Bond Finance, says, ***“Jefferson County is a relatively isolated incident relative to the overall municipal market and all of the disclosure in the world ... helps financial mismanagement”*** He goes on to argue, ***“SEC ought to have other priorities in terms of where ... to spend their time, effort and energy protecting investors.”***
- Frank Hoadley, Wisconsin's Capital Finance Director and Chair of GFOA Debt Committee offers his words of wisdom attributing the ARS problems largely the result of investors not reading the documents. ***“There's an old saying in the municipal bond market that buyers don't read and readers don't buy.”*** Hoadley goes on to state, ***“They didn't bother to read the disclosure documents, and I'm not aware of any that didn't spell out the risks”***

Why SEC and the Market Shouldn't be Worried

- Local agencies didn't create the current mess
 - Remember our motive is not financial greed
 - Our motive is providing affordable capital to finance quality public facilities
- Our constituents – the PUBLIC have long, long memories when public funds are lost or mismanaged; some public servants operate in the shadow of the predecessors for decades

Why SEC and the Market Shouldn't be Worried

- We live in “Glass Houses”
- Strong Professional Organizations such as GFOA Recommended Practices
 - Method of Sale
 - Selecting Professionals – Financial Advisor, Underwriter, Bond Counsel
 - Post-Issuance Check List
- Focus where the issues really are ...
 - Dishonest and unqualified professionals
 - Few “bad apples” – issuer side of the market isn't broken
- Give EMMA a chance

San Jose Experience -- Last Six Months of Debt Management

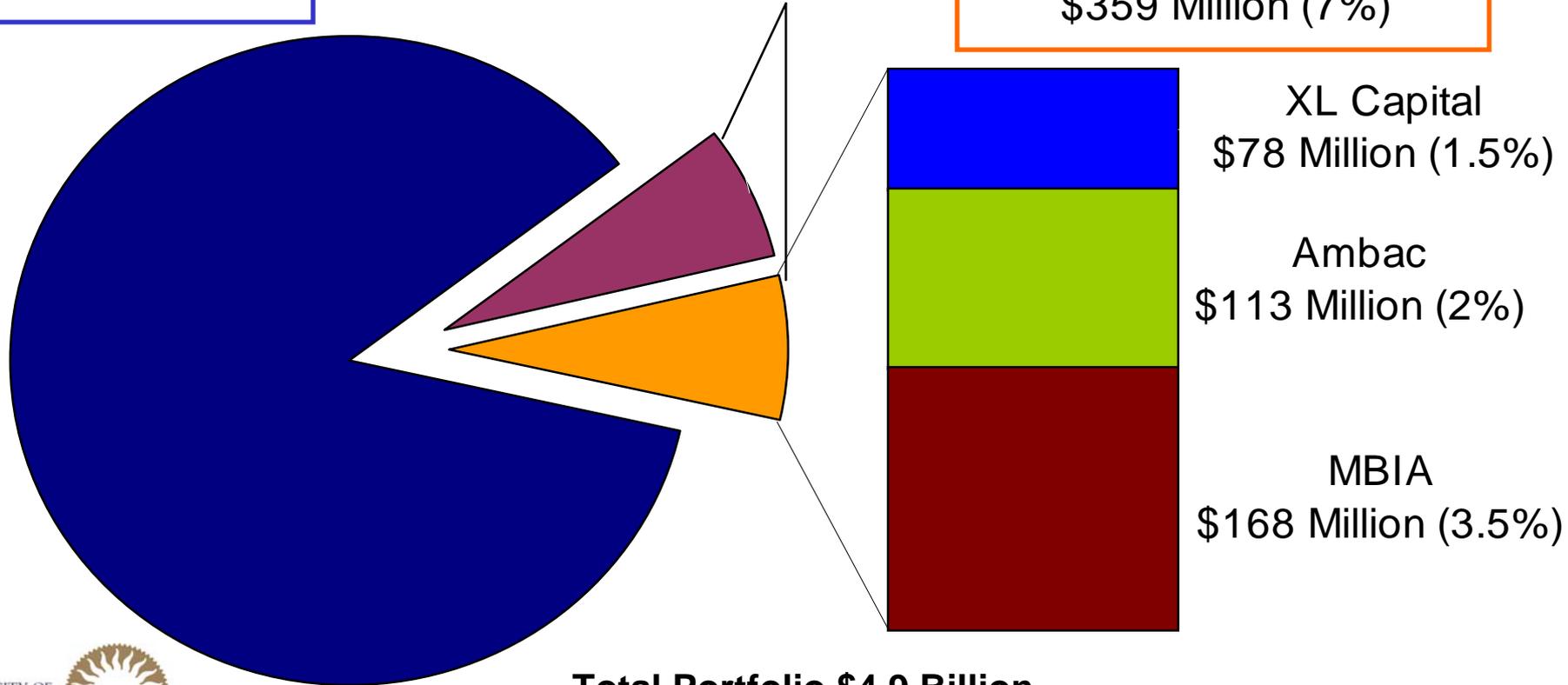
- Nearly \$5.0 billion debt portfolio
- **Good News** only 7% or \$360 million of portfolio was variable rate debt with bond insurance exposure
- **Bad News** – represented eight separate series of bonds
 - Budgetary impact was mounting
 - Pressure to complete refundings/restructurings by end of fiscal year

Majority of Portfolio Not Impacted

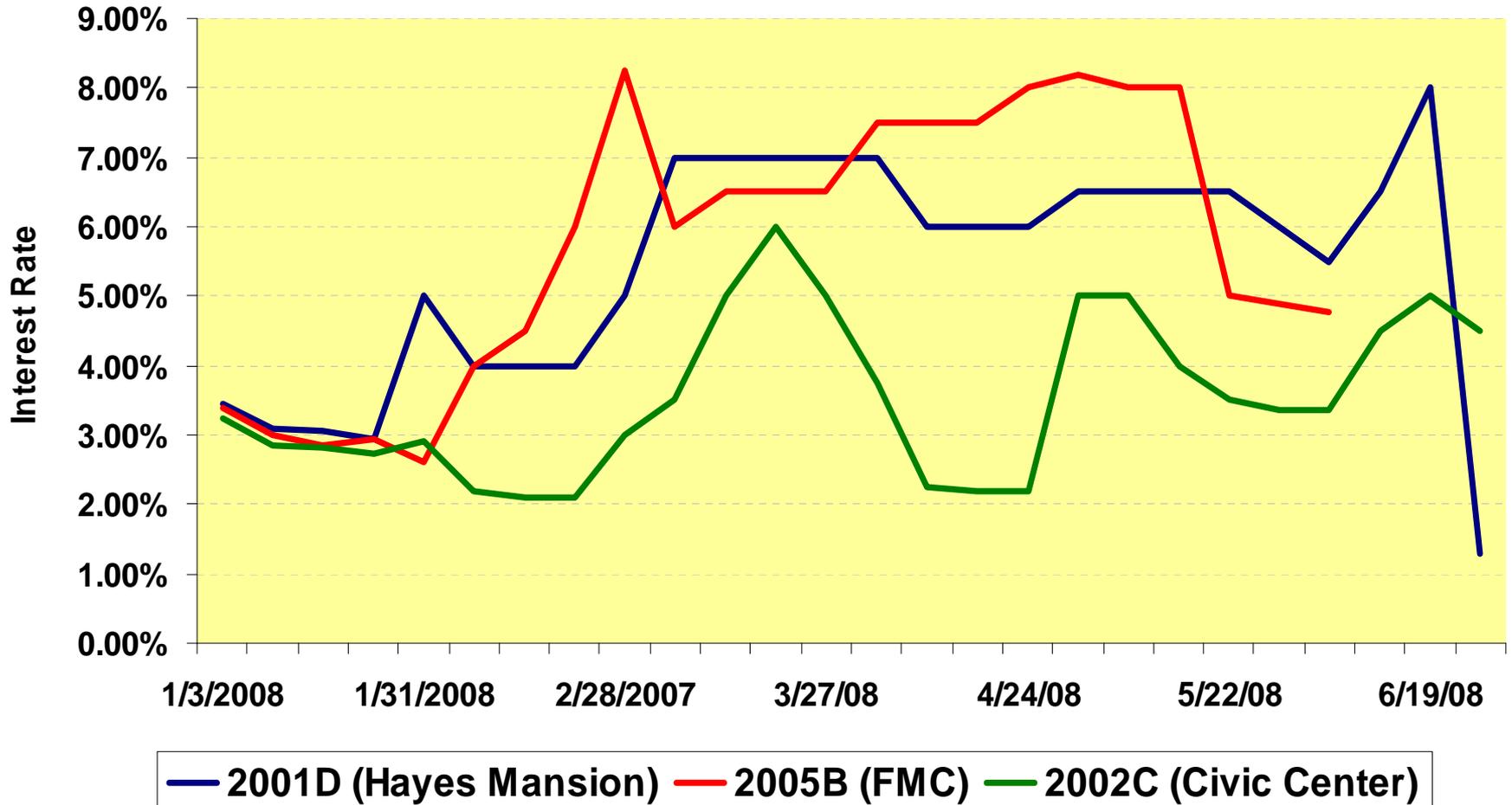
Fixed Rate Debt
\$4.2 Billion (86%)

Variable Rate Debt
\$678 Million (14%)

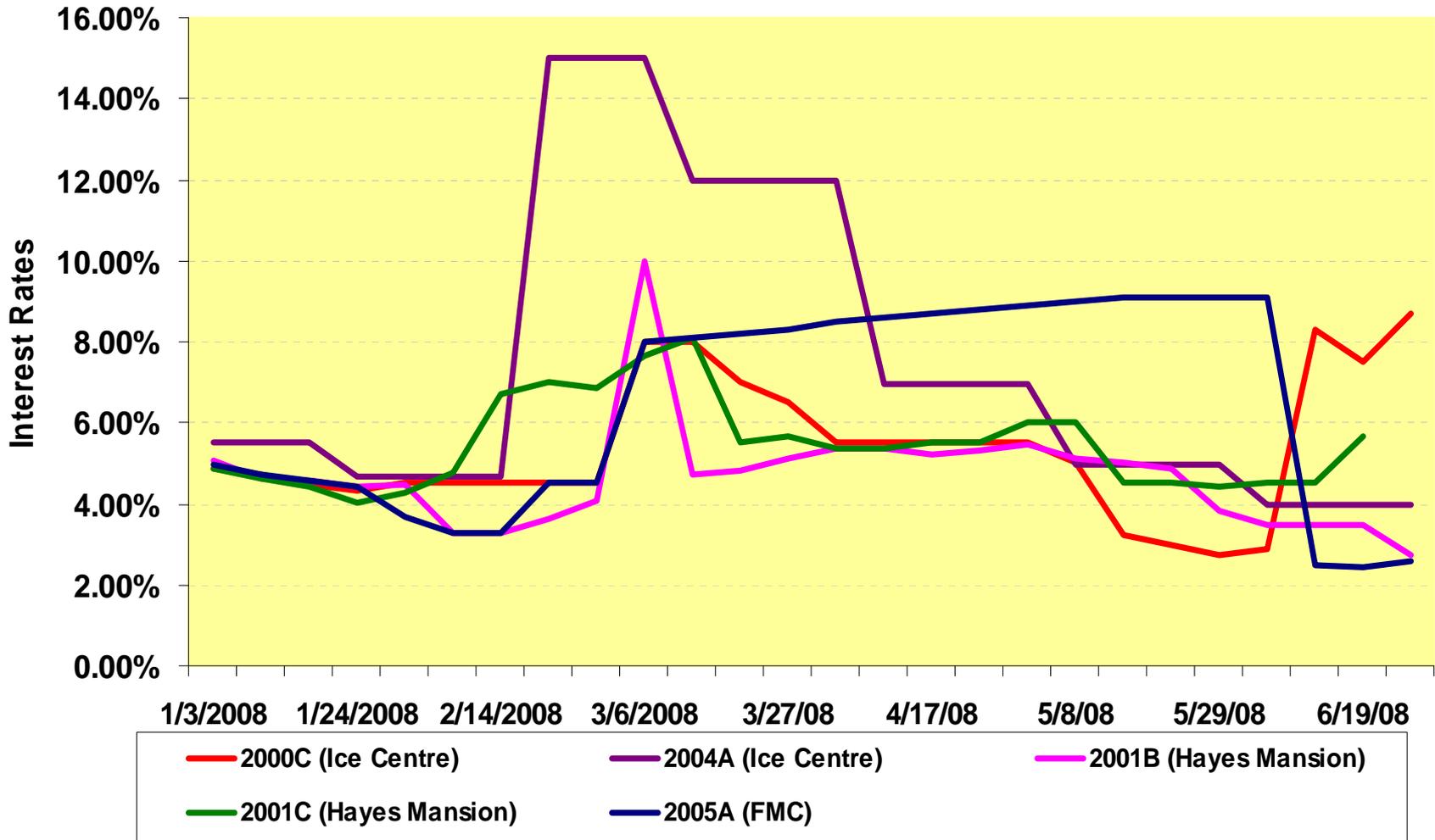
Variable Rate Debt with
Bond Insurance Exposure
\$359 Million (7%)



City of San Jose Financing Authority Tax-Exempt Variable Rate Debt (Jan – June 2008)



City of San Jose Financing Authority Taxable Variable Rate Debt (Jan – June 2008)



Good Disclosure – Issuers Need to Care

- **Disclosure is the CITY'S responsibility**
 - Cannot rely on consultants – be active & involved
 - Disclosure is hard work and is NEVER done
 - Critical to success or failure in marketplace
 - Never exciting to anyone else
 - Must be tenacious and persistent
 - Continually looking for ways to streamline process
- **Balancing Act** for competing resources
- **Approach with caution** when undertaking a new financing structure or vehicle
- **Good Disclosure: It's IN the Process**