POOLED MONEY INVESTMENT BOARD
915 Capitol Mall, Room 110
Sacramento, CA 95814

MINUTES

Wednesday, October 20, 2004

The meeting was called to order at 10:00 a.m.

Roll:	Carrie Cornwell for State Treasurer Philip Angelides Cindy Aronberg for State Controller Steve Westly Bob Campbell for Interim Director of Finance Michael Genest
Staff Present:	Mark Paul, Executive Secretary, PMIB Doug Spittler, State Treasurer's Office Connie LeLouis, Attorney General's Office Linda McAtee, State Treasurer's Office

APPROVAL OF MINUTES

The Minutes for the meeting of September 15, 2004, were approved as submitted, 3-0.

APPROVAL OF PMIB DESIGNATION NO. 1664

Mr. Doug Spittler of the State Treasurer's Office presented the portfolio Summary Report as of October 12, 2004. On that day, the portfolio stood at $52.185 billion. The effective yield was 1.881%, the quarter-to-date yield was 1.870%, and the year-to-date yield was 1.701%. The average life of the portfolio was 194 days and AB 55 Loans approved stood at $4.569 billion with $1.081 billion having been disbursed. The Local Agency Investment Fund had deposits totaling $19.459 billion with 2,750 participants.

Mr. Steve Muraki, of the Cash Management Division of the State Treasurer's Office, presented a summary of the Forecast of Changes in portfolio for the Pooled Money Investment Account for the period October 18, 2004, through December 17, 2004. He stated that over the nine-week period of the forecast, there would be an increase in the portfolio of $4.514 billion due to receipts exceeding disbursements. Mr. Muraki continued by highlighting several of the key receipts. He noted that the Sales, Liquor, and Utility Surcharge were expected to total $7.551 billion and that Motor Vehicle Fuel Taxes were anticipated to total $417 million. Personal Income and Bank & Corporation Taxes were expected to total $6.971 billion. The Insurance Gross Premium Taxes were anticipated at $425.7 million, while the proceeds from the Sale of State Bonds were expected to total $1.669 billion. For this nine-week period, $31.383 billion was anticipated in receipts.

Mr. John Korach of the State Controller's Office presented the Estimated Pooled Money Disbursements for the forecast period and highlighted several of the major disbursements. Public Schools and Community Colleges were expected to have a disbursement of $1.9 billion on October 27th and another $1.7 billion disbursement on November 22nd. Social Services had a major disbursement of $835 million scheduled for the week of October 25th with another $665 million scheduled for the week of November 29th. Health Care Services were expected to disburse $400 million each week for Medi-Cal during the nine-week period for a total of $3.6 billion. Payroll Revolving Fund payments were scheduled to be made on November 1st for $1.2 billion and again on December 1st for $1.2 billion. Debt Service was estimated to have a disbursement of $946 million during the week of November 1st and another $591 million in the week of November 29th. Mr. Korach concluded by stating that the major disbursements for the nine-week period were estimated at $25.912 billion.

Designation No. 1664 was approved, 3-0.

APPROVAL OF AUTHORIZATION FOR GENERAL FUND INTERNAL BORROWING

Mr. Doug Spittler presented this document which authorizes the General Fund to borrow from internal sources – the special funds and accounts within the State Treasury – to meet its cash needs during periods of shortfall. The authorization presented at this meeting was for the period November 1, 2004, through January 31, 2005. He noted that the amount available from various internal funds was estimated to be $9.578 billion.

The Authorization for General Fund Internal Borrowing for the period November 1, 2004, through January 31, 2005, was approved, 3-0.

APPROVAL OF SURPLUS MONEY DECLARATIONS/REDUCTIONS

Mr. Doug Spittler presented the changes in the Surplus Money Investment Fund for the period September 1, 2004, through September 30, 2004. During that month, $7.256 billion was declared surplus in various special funds, while $7.486 billion was declared to be a reduction in surplus.

The Surplus Money Declaration/Reduction for the month of September 2004 was approved, 3-0.

APPROVAL OF SURPLUS MONEY INVESTMENT FUND REQUESTS

Mr. Doug Spittler presented three SMIF requests. The first request was from the Department of Consumer Affairs for the Athletic Commission Fund (Fund Number 0326). The second request was from the San Francisco Bay Conservation and Development Commission for the Special Deposit Fund, Gateway Park Public Access Fund (Fund Number 0942158). The third request was from the Department of Consumer Affairs on behalf of the Bureau of Naturopathic Medicine for the Naturopathic Doctor's Fund (Fund Number 3069). Mr. Spittler said that staff had reviewed these requests and recommended them for approval.

The Board accepted the staffs' recommendations and approved the three requests, 3-0.

APPROVAL OF AB 55 LOANS

Mr. Chris Kooyman of the Public Finance Division of the State Treasurer's Office presented the sixteen loan requests under agenda item #7 as shown in the following table. Mr. Kooyman noted that loans 7.a. through 7.d. were for general obligation bond programs and that loans 7.e. through 7.p. were for lease revenue bond programs.

Loan Number	Type	Department/Program	Adjusted Loan Amount
045058	GO/Renewal	California State University Public Education Facilities Bond Act of 1996 (Hi-Ed)	$936,827.97
045059	GO/Renewal	Water Resources Control Board for Department of Water Resources Safe, Clean, Reliable Water Supply Bond Act of 1996	$40,411,846.15
045060	GO/Renewal	Resources Agency Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002	$129,442,046.00
045061	GO/New	California Community Colleges Kindergarten-University Public Education Facilities Bond Act of 2004 (Hi-Ed)	$30,000,000.00
045062	REV/Renewal	Department of Forestry & Fire Protection SPWB Lease Revenue Bonds Dew Drop Forest Fire Station	$85,330.00
045063	REV/Renewal	Department of Forestry & Fire Protection SPWB Lease Revenue Bonds Pacheco Forest Fire Station	$60,700.00
045064	REV/Renewal	Department of Forestry & Fire Protection SPWB Lease Revenue Bonds Hemet-Ryan Air Attack Base	$38,000.00
045065	REV/Renewal	Department of Forestry & Fire Protection SPWB Lease Revenue Bonds Manton Forest Fire Station	$2,435,000.00
045066	REV/Renewal	Department of Forestry & Fire Protection SPWB Lease Revenue Bonds South Operations Area Headquarters	$520,000.00
045067	REV/Renewal	Department of General Services SPWB Lease Revenue Bonds State Office Buildings #8 and #9 Renovation	$8,077,520.00

APPROVAL OF AB 55 LOANS (Continued)

Loan Number	Type	Department/Program	Adjusted Loan Amount
045068	REV/Renewal	Department of General Services SPWB Lease Revenue Bonds Bonderson Building Renovation	$1,200,000.00
045069	Rev/Renewal	Department of Mental Health SPWB Lease Revenue Bonds Atascadero State Hospital: Multi-Purpose Building	$13,220,000.00
045070	REV/Renewal	Department of Mental Health SPWB Lease Revenue Bonds Patton State Hospital: Upgrade Electrical Generator Plant	$168,000.00
045071	REV/Renewal	Department of Mental Health SPWB Lease Revenue Bonds Patton Hospital: EB Bldg. – Fire/Safety/ Environmental Improvements Ph. 2 & 3, Renovate Admission Suite	$619,000.00
045072	REV/Renewal	Department of Justice SPWB Lease Revenue Bonds Santa Barbara Replacement Laboratory	$6,100,000.00
045073	REV/Renewal	Department of Corrections SPWB Lease Revenue Bonds California State Prison – San Quentin, Condemned Inmate Complex	$11,624,045.00

Mr. Kooyman said that all loans were recommended for approval as presented and that the impact on the Pool would be to increase AB 55 loan balances by $29.3 million.

All sixteen loans were approved in the amounts recommended by staff, 3-0.

APPROVAL OF ENERGY EFFICIENCY AB 55 LOANS

The Chair, Ms. Carrie Cornwell, said that Mr. Juan Fernandez of the Public Finance Division of the State Treasurer's Office would present these three loans.

Mr. Fernandez stated that at the request of the Department of Finance, the agenda for today's meeting includes renewals for three outstanding loans for the State Public Works Board's Energy Conservation Revenue Bond Program. These loans were originally to be repaid with the proceeds of a bond sale scheduled for November 2004. He indicated that some background would be helpful.

Normally, the AB 55 loans approved by this board for revenue bond programs are secured by:

1. The authority and ability of the borrowing agency to issue bonds.
2. The Legislature's pledge of the support appropriation of the borrowing agency, if bonds cannot be sold. Under this provision, the Treasurer's Office (as staff to the board) would instruct the Controller to tap into the borrower's support appropriation to repay the loan (principal and interest).

Last month, the Attorney General's Office informed us that it could not deliver its usual and customary validity opinion for the Energy Conservation Bond Program. Without that opinion, the Treasurers' Office could not sell the bonds and was ready to instruct the Controller's Office to transfer sufficient funds from the borrowers' support appropriations to repay the loans. However, prior to our doing this, a request came from the Department of Finance to put these loans on the agenda for this meeting. Finance also requested that these loans be renewed for six months in order to give them time seek a deficiency appropriation to repay the loans.

The three loans in question, indeed all of the AB 55 loans granted to date, have been made under Government Code Section 16312, which provides that the Board may make a loan from the Pooled Money Investment Account to any special fund for the purpose of carrying out a program or project that is authorized to be financed by issuing bonds, notes, or other evidence of indebtedness.

Clearly, the Energy Conservation Revenue Bond Program is no longer "a program or project that is authorized to be financed by issuing bonds, notes, or other evidence of indebtedness." In our view, these loans cannot be renewed under the legal authority used since the inception of the AB 55 loan program.

However, the Attorney General's Office informed the Board, in a memo dated October 14, 2004, that there was another Government Code Section (§16313) under which the renewal of the loans could be granted.

The purpose of Section 16313 was to allow the Board to provide replacement financing for state agencies that had entered into equipment leases at high interest rates, when the Board determines that it is in the best interest of the state to do so. To our knowledge, the Board has never granted a loan under this Government Code section.

So, the Board has two options before it regarding these three Energy Conservation Revenue Bond Program loans:

1. Instruct the Controller's Office to transfer funds from the borrowers' support appropriations to repay the loans; or
2. Renew the loans under Government Code Section 16313.

Our recommendation would be to repay the loans from the departments' support appropriations. This is not new. In fact, it has happened twice since I have been in this position. Our recommendation was made for the following two reasons:

1. It is critical, in our view, that the Board be comfortable with the fact that when bonds cannot be sold to repay a loan that the Treasurer (on the Board's behalf) will be able to tap, without any further administrative action, an agency's support appropriation to get these loans repaid.
2. With all due respect to the Attorney General's Office, it seems to us that Section 16313 does not apply to the current situation. In our view, these are not high interest rate loans that need to be refinanced for the sole purpose of lowering the interest costs of the borrowing agencies.

However, we acknowledge that this decision involves a policy issue that the Board needs to address. If the Board chooses to refinance these three loans under the provisions of Government Code Section 16313, we request that it do so under the following three conditions.

1. The term of these loans should be for a short period—say four months or so.
2. The Department of Finance should be required to certify that sufficient funds would be available from the borrowing departments' support appropriations when the loans come due.
3. The Board should make it clear that, if Finance has not obtained a deficiency appropriation to repay the loans by the time the loans come due, the Treasurer will instruct the Controller to transfer funds from the departments' support appropriations to repay the loans.

Ms. Cornwell thanked Mr. Fernandez for his presentation and asked Mr. Mark Paul if he had any comments that he wanted to make?

Mr. Paul stated the Board had a fiduciary responsibility to the Pool—an obligation to act solely in the interest of the Pool. We're managing other people's money and we have a duty to manage the Pool's assets as if the Pool participants were prudently managing it themselves. As Juan indicated, we believe that Section 16313 was intended to take out high interest rate loans with the lower rates available under the AB 55 Loan Program. The borrowing agencies would, therefore, be able to repay the new loans with the savings that would accrue to their support appropriations due to the lower interest charges. It is our understanding that none of these departments currently have appropriations that support higher interest payments and, therefore, there would be no savings to repay the Section 16313 loan. The only security for repayment of these new loans would be the expectation that the Legislature would approve a deficiency appropriation or that we could, later in the fiscal year, after more of the departments' funds are exhausted, tap their support appropriations. In our judgment, this adds an element of risk to these loans (and, therefore, the Pool) that was not originally intended by the Legislature when it passed Section 16313. We believe that granting these loans would not meet our fiduciary duty and that these loans would likely cause concern among the local agencies with money invested in the

Pool. These agencies are very sensitive to any perception that the state is borrowing their money to solve the state's own budget problems. Staff recommends that these loans be denied.

Ms. Cornwell thanked Mr. Paul for his statement and asked if there were any comments from the Board members?

Mr. Bob Campbell indicated that he did have some comments to make. He stated that he appreciated the comments and concerns expressed by the Treasurer's Office. He said that it was Finance's request that the loans be renewed on a limited-term basis. We do not believe that the risk to the fund is of a nature that warrants denial of the renewals. The inability to sell the bonds to repay the loans was completely unforeseen by all of the departments involved. If the Board calls these loans, thereby requiring repayment from the departments' support appropriations, the departments will need to take immediate actions to reduce programs and services to the public. We think that the disruptions that this would cause over the short period are unwarranted. We are working with the Legislature to seek a new appropriation to take care of the loan repayments, and, in light of that fact, I think that it is most appropriate to renew these loans under the conditions Mr. Fernandez indicated. First, however, I would like to confirm with Finance staff that we would be okay with these three conditions.

Ms. Aronberg expressed reservations with the third condition proposed by Mr. Fernandez. It seemed to her that the Board should have another meeting on these loans, instead of just calling them, if Finance is unable to obtain a deficiency appropriation to repay the loans.

Mr. Campbell concurred with the concern raised by Ms. Aronberg.

Mr. Fernandez responded by stating that the third condition already exists—that the State Treasurer's Office has the authority to direct the Controller's Office to tap the support appropriations of the departments when the STO deems the loans to be bad. We just wanted to make sure that the Board was clear on this fact and to make a public statement that when the loans become payable, if the DOF has been unable to obtain a deficiency appropriation, then there would be no question that the STO would go forward and get these loans repaid by directing the SCO to tap their support appropriations. He was sorry if he did not make this point clear during his presentation.

Ms. Aronberg responded by stating that the Board meets in a regular monthly meeting and could always call an interim meeting, if necessary. Furthermore, since interest continues to accrue, there would be no risk to local agencies. Whenever the loans are repaid, they will be repaid with interest—whether it is right after the Legislature gets in session or a little longer—but ultimately the interest will be repaid. She concluded by stating that she thought the Board should review these loans again before calling them, if calling them becomes necessary.

Mr. Campbell stated that it was Finance's view as well that these loans should be brought back to a future meeting. At this meeting, the Board would know what the likelihood of a deficiency appropriation was and whether or not there was a need to take action.

Ms. Aronberg stated these loans should be brought back to the PMIB meeting immediately preceding the date which the Board sets today as the repayment deadline, or sooner, if staff see a need for it.

Ms. Cornwell indicated that she thought Mr. Fernandez was saying that if the Board were to grant an extension of these loans, or renewal of these loans, or new loans, or whatever, that they do not necessarily have to come back here, that the existing statutory process could be invoked at that time—so maybe it is a legal question. Staff, was there some other comment that you wanted to make?

Mr. Spittler responded by stating that we have exercised the right to attach a department's support appropriation several times in the past and under no circumstances has the exercise of this provision required returning to the Board. If you decide that we now have to have a second meeting to determine if we want to exercise this provision, you may be jeopardizing the whole revenue bond loan program. Currently, when the Public Finance Division staff recommends approval of a loan to the Board, they are stating that there is nothing in the way to prevent repayment of this loan. Does this set a precedent that we should bring everyone of these loans back to the Board, and if so, would staff be doing their duty if they recommended approval of any loans requiring this contingency language that now apparently cannot be exercised?

Mr. Campbell stated that he did not think that there was any question with regard to the STO's authority to exercise this repayment provision and that he would not view this proposal as precedent setting. He thought that under the unique circumstances involved here that renewing the loans for a brief period, in order to get a deficiency appropriation through the Legislature to avoid program or service disruptions, was a prudent course of action for the Board to take.

Mr. Spittler stated that he thought that there was still a risk to the Pool due to the over $19 billion of local agency money held in the Pool. Perception of safety is very important to the local agency participants. Just rumors can cause significant disruptions to an investment program. If this proposed action were perceived by the local agencies to give special treatment to the state, it would not be unheard of to see some sort of a run on the local agency deposits. This would be especially true since you would be seeking specific legislation to fund this deficiency and would be going before legislative committees describing exactly what has gone on. Therefore, this action would likely become fairly well known among most of the local agency investment community in California and could result in significant pullouts of local monies.

Mr. Campbell responded by stating that their primary concern was with the third condition proposed by Mr. Fernandez and that the four-month period suggested as the first condition might not allow sufficient time, given the short time that the Legislature would be back in session, to get a new appropriation bill through the Legislature. He suggested that one possible alternative might be to authorize a six-month term for the loan rather than a four-month one. This would allow more time for the legislative process to work and would perhaps make the third condition more acceptable.

Ms. Cornwell asked Ms. LeLouis if these actions would be extensions or renewals or what? She understood Mr. Fernandez to say that all prior AB 55 loans were made under one code section and that based on the opinion of the A.G.'s Office, these three loans would be made under a different code section.

Ms. LeLouis indicated that this was correct.

Ms. Cornwell continued by asking if these would be new loans or renewals?

Ms. LeLouis stated that she had been waiting for a chance to clarify this issue. She continued by saying that the legal effect was probably that these loans look like they have been renewed, but practically speaking the statute under which they may be made is a different code section. This section, §16313, will require the Board to make different findings and these loans would, therefore, be new loans issued to replace existing loans issued under §16312.

Ms. Cornwell then asked what finding the Board would specifically need to make to grant new loans under §16313?

Ms. LeLouis responded by reading the first paragraph of §16313:

> *Notwithstanding and in addition to any other provision of law permitting loans to state agencies from the Pooled Money Investment Account, the Pooled Money Investment Board may make a loan, on such terms and conditions as the board may determine, from the Pooled Money Investment Account to any state agency in order to prepay or replace existing financing when the board determines it is in the best interest of the state to do so. Interest on the loans shall be determined as provided in Section 16314.*

Ms. LeLouis continued by stating that the Board would have to make a finding on the record that it was in the best interest of the state, and if the Board were to do that she would like the Board to articulate why just for purposes of making the finding. The Board should then impose whatever terms and conditions it thinks would be appropriate to make these loans because they would be replacing existing loans made under a different code section and it is her understanding from staff of the Treasurer's Office that this new code section has not been used before this time.

Ms. Cornwell replied that, as she understood it from the presentation, this new section was intended to be used in the specific circumstance where there would be an interest rate advantage to using it.

Ms. LeLouis answered by stating that while the legislative history of a statute may support why a statute was enacted, the history would not usually help define the scope of a statute unless there were ambiguities with the statute; and on it's face, §16313 would appear to be pretty straight forward in terms of what it would authorize. So, while the history would provide interesting background, it would not be controlling because a court would never get to the legislative history where the statute, on its face, was pretty clear about what it would allow. She continued by stating that there seemed to be authority in their view under §16313 for the Board to make these new loans, if the Board chose to do so. She concluded by stating that was what they were asked to give advice to the Board about.

Mr. Campbell stated that he certainly thought that the Board could make a finding that authorizing these new loans would be in the best interest of the public. This would be due to the unforeseen nature of the inability to sell the bonds and the significant potential for a disruption in programs and services to the public, if the support appropriations should be tapped in these departments.

Ms. Cornwell then asked if there were any other comments?

Mr. Fernandez then responded that from a staff point of view, whether it is four months or six months, he would like the Board to understand our concern. He stated that the longer you go into the fiscal year—and maybe the SCO can speak to this issue—the less money there would be available in the support appropriation to repay the loans. Therefore, it would be critical that the Board get the certification from the DOF that on the due date, whether it would be four months away or six months away, there will be enough funds remaining in the support appropriation for those departments to repay these loans. We would not want to be in a situation where six months from now when these loans would come due and the Department of Finance was unable to get a separate deficiency appropriation that there would not be enough money in the support appropriations to repay these loans. He stated that was critical for the Board to obtain that certification.

Ms. Cornwell asked if the SCO wanted to comment on this issue?

Mr. John Korach indicated that he was in agreement with Mr. Fernandez's comments. He stated that we might want to consider other options during that six-month period. As the year progresses, expenditures occur and your support appropriation dwindles. He added that perhaps a block on the funds could be placed to ensure that the funds would be available to repay the loans should alternative financing not come through.

Ms. Cornwell indicated that she would like to make a comment. Certainly the Department of Finance has identified this situation as being unique and that it has created a budgetary problem that must be dealt with. They propose to solve this problem by pursuing a legislative solution. She continued by stating the Treasurer believes that we, in our roles as Pooled Money Investment Board members, need to act as fiduciaries of the Pool, to act almost solely in the interest of the Pool. Thus, our responsibility and our role as PMIB members would be to exercise the same, skill and diligence with the funds of the Pool that any prudent investor with a similar-sized asset would exercise. She further stated that she would not be voting today to renew or approve these loans even with the previously discussed conditions. She added that it was the STO's opinion that the PMIB members should be evaluating these loans under Government Code Section 16313 as to whether they would be in the best interest of the Pool. She stated that in the Treasurer's judgment and in the STO's judgment that the best interest of the Pool outweighed the budgetary issue that has been raised here today and that for this reason she would not be joining in the vote, which sounds like would be before us shortly. She concluded by asking if there were any other comments?

Mr. Campbell then moved, under the conditions expressed by Mr. Fernandez, to enter into new loans for a period of six months with the finding that this action was in the best interest of the state in light of the unforeseen circumstances involved and the adverse consequences that would result from a reduction of programs and services to the public.

Ms. Cornwell then asked if there was a second?

Ms. Aronberg responded that she had a quick comment and then she would second the motion. She stated that she strongly believed that there was no fiduciary problem with approving these loans given that interest would continue to accrue to the Pool and that the Pool would, therefore, not be in any worse shape because of these loans. She concluded by stating that she strongly disagreed with the STO's contention and that she would second the motion.

Mr. Campbell stated that he agreed with Ms. Aronberg's final comment.

Mr. Kooyman then said that he needed to present the details of the three energy bond loans to the Board:

Loan Number	Type	Department/Program	Adjusted Loan Amount
045074	REV/New	Department of General Services SPWB Energy Conservation Revenue Bonds Secretary of State Archives Building	$1,145,143.00
045075	REV/New	Department of Corrections SPWB Energy Conservation Revenue Bonds Avenal State Prison	$7,687,409.00
045076	REV/New	Department of Corrections SPWB Energy Conservation Revenue Bonds Chuckawalla Valley State Prison	$3,093,300.00

Ms. LeLouis then asked, for her own clarification, if they were moving with the conditions or not.

Ms. Cornwell responded yes, with the conditions presented by Mr. Fernandez, but for a term of six-months rather than four-months. She then stated that if there were no other comments, questions, or clarifications, she would ask the clerk to please call the roll on the motion to approve these three loans.

State Treasurer:	No
State Controller:	Aye
Director of Finance:	Aye

The three loan requests were approved in the amounts recommended by staff under the conditions described above, 2-1.

PUBLIC COMMENT

None.

In the absence of further business, the meeting was adjourned at 10:38 a.m.

Respectfully submitted

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Mark Paul
Executive Secretary