

California Debt and Investment Advisory Commission

Fundamentals of Debt Financing Initial Disclosure

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October 3, 2008



STONE &
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Initial Disclosure

Balance between marketing of securities and importance of disclosing pertinent risks and information to investors



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The Basic Laws Requiring Disclosure

- **Common Law of Deceit or Fraud or Breach of Fiduciary Obligation**
- **Federal Securities Laws**
 - ✓ Securities Act of 1933, Section 17(a)
 - ✓ Securities Exchange Act of 1934, Section 10(b)
 - ✓ SEC Rule 10b-5
 - ✓ SEC Rule 15c2-12

No Secrets



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General Disclosure Items

Often in the 1st Part of the Official Statement

- ✓ Introduction of the Offering expressed in “plain” English
- ✓ Description of the Security and Nature of the Obligation
- ✓ Legal Authorization to Issue debt and Purpose of the Issue
- ✓ Discussion of how the security will be registered and tracked
- ✓ Statement on Continuing Disclosure that will be undertaken
- ✓ Description of Default remedies
- ✓ Legal and Tax Matters
- ✓ Litigation and Resolutions
- ✓ Risk Factors/Special Considerations for the investor
- ✓ Professionals Involved in the financing

Due Diligence

- ✓ Document Review Sessions
- ✓ Due Diligence Meeting
- ✓ Due Diligence Visit to Borrower by Counsel

Demographic / Economy Items

Often in the 1st Part of the Official Statement (sometimes in an Appendix)

- ✓ General history of the issuer
- ✓ Description of the Governmental Structure & Organization
- ✓ Issuers Budget process as it may effect the repayment of debt
 - Voter approval requirements, financial controls and monitoring provisions.
- ✓ Identification of key leadership and administrative personnel
- ✓ General description of the economic base
 - Land use, major industries, and land use limitations
- ✓ U.S. Census Bureau Data – Last 4 Censuses & Current Estimates
 - Population data, breakdown of percentage of population by age, average annual income, and wealth levels
- ✓ Construction Statistics
- ✓ History of retail sales
- ✓ Top 10 employers and tax payers
- ✓ 10 years of annual unemployment statistics

Financial Statements

Most recent annual audited financial statements, with Notes and the auditors opinion must be accompanied with the Official Statement (most often this is in an Appendix)

Additional information that should be included if not in the Audit

- ✓ Period of availability used for recognition of revenues in financial statements
- ✓ Detail of significant individual receivables and payables
- ✓ If the disclosure document is being prepared in the Q4 of a fiscal year, a budget based estimate of that fiscal year's results as well as the adopted budget for the next fiscal year should be included
- ✓ Current year's summary budget and subsequent year's budget, if adopted
- ✓ Historic general fund financial information and performance
- ✓ The date or dates at which GASB 34 was or will be implemented
 - A discussion of which capital assets are being depreciated and how they will be valued if other than on the basis of historic records

General Revenue Base

Often in the 1st Part of the Official Statement (sometimes in an Appendix)

- ✓ Major Revenue Sources
 - ✓ Any category of revenue that represents more than 15% of the source of fund revenues, or the top 5 revenue sources, whichever is larger should be disclosed separately
 - ✓ Legal basis for the revenue, and method of assessing the revenue
 - ✓ Five years of historical data for all relevant revenue sources
 - ✓ Major changes – historical or projected in revenue sources
- ✓ Property Tax
 - ✓ General nature of the property tax base – breakdown of property valuation
 - ✓ Five year property tax history, including tax rates, collections and delinquencies
 - ✓ An explanation of any property tax appeals process and any pending appeals
- ✓ Sales Tax
 - ✓ Legal basis for collection of sales tax
 - ✓ Table of last 4 years of total receipts and sales tax rates
 - ✓ Major sales tax payers
- ✓ Other Revenue and Financing Sources (i.e. Income Tax, TOT ...)
 - ✓ Similarly must disclose (legal basis, historical receipts, and concentration issues)

General & Other Expenditures

Often in the 1st Part of the Official Statement (sometimes in an Appendix)

- ✓ For each item as seen on the statements of revenues and expenditures, a short explanation of the composition of the item as well as information about any trends
- ✓ Debt service payments (P&I)
- ✓ Legal basis for any expenditures that are driven by changes in revenue
- ✓ Any information regarding the possible automatic changes to any expenditure category in the event of a revenue shortfall
- ✓ Description of Pension Plans – GASB Statement 25, the pension plan's required supplementary information should be included in the body of the disclosure document
- ✓ OPEBs – a discussion of other post retirement benefits, away from pensions benefits, and compliance with GASB 45

Debt & Financial Obligations

1st Part of the Official Statement

Include any obligations that may have been issued by another entity if the repayment obligation is or could be that of the entity responsible for the disclosure document

- ✓ Amount of authorized debt
- ✓ Itemize all outstanding long-term debt and other capital financial obligations that are secured by GF revenues
- ✓ For short-term obligations – provide information going back at least five years
- ✓ Separately, identify other forms of debt outstanding that not necessarily backed by GF
- ✓ Information about any “loans” related to governmental agencies
- ✓ Statement of legal debt limitation
- ✓ Direct and Overlapping debt of the issuer
- ✓ Total Debt Service Schedule
- ✓ Any existing swap terms or information with respect to the bonds of the issuer

Cash Flow Financing

1st Part of the Official Statement

- ✓ For the last two fiscal years, comparison of each year's operating budget to actual results, accompanied by a discussion of the assumptions used in preparing the original budgets
- ✓ Cash flow statement for the current fiscal year vs. the period prior
- ✓ Quarterly Cash Flow Statements (cash flow financings only)
- ✓ A comparison of forecasted to actual cash flows for the prior two fiscal years including a discussion of material variances
- ✓ Discussion of the assumptions used in the development the cash projections
- ✓ Sufficient detail to identify major sources and uses of cash receipts which are available to pay debt service or pay working capital expenditures in lieu of financing proceeds
- ✓ A full description of how balances and bond proceeds will be invested
- ✓ To the extent the issuer has the legal ability to borrow internal or external resources to cover any cash flow deficit

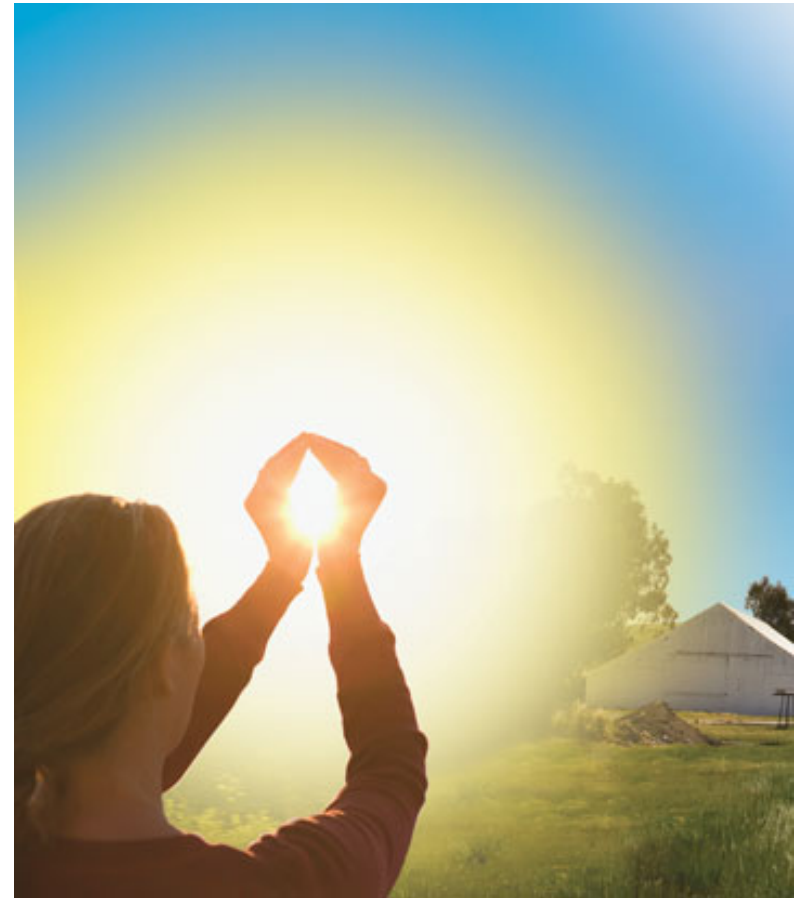
What's Coming?

MSRB substitutes for NRMSIRs

- ✓ Initial and continuing disclosure
- ✓ Electronic “access equals delivery”

Underwriter delivers OS by closing date

Coming “in the near future”





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