

Attachment “E”

as provided by
the

Treasurer-Tax
Collector

TREASURER’S REPORT ON STATE REGISTERED WARRANTS AND OTHER RELATED IMPACTS ON THE COUNTY TREASURY

July 10, 2009

The Treasurer’s office is an integral component of the countywide process of receiving revenue and paying out authorized expenditures. On any given day the Treasurer may deposit and pay out amounts ranging from \$1 million to as much as \$100 million (when large bond payments are due coupled with school/county payrolls). To ensure sufficient cash is always available to meet multi-agency demands, the Treasurer maintains a robust cash management program that has historically provided ample liquidity that anticipates both incoming revenue and outgoing payments. The onset of the State budget crisis along with the ongoing recession has disrupted the ability to accurately and timely anticipate the required cash needs for all depositors in the county treasury. Those depositors are generally comprised of:

* Schools	60%	of treasury assets	(\$600 million)
* Special Districts	10%	“ “	(\$100 million)
* County General Fund	12%	“ “	(\$120 million)
* Other County Funds	18%	“ “	(\$180 million)

Total assets in treasury \$1 billion

There are no city or out of county depositors in the county treasury.

This analysis of the impact of the State crisis on the county treasury considers:

- I. DEFERRED STATE PAYMENTS**
- II. ISSUANCE OF REGISTERED WARRANTS (IUO’S)**
- III. OTHER PUBLIC AGENCY ISSUES**

Although there are significant economic and State budget impacts on the cash flows of schools and special districts, the focus of deferred State payments and Registered Warrants will be on the County of Monterey. The section on “Other Public Agency Issues” will discuss how outside agency cash shortfalls could involve the county treasury.

I. DEFERRED STATE PAYMENTS

At the time of this report, the State has notified affected counties (those over 40,000 population) of the deferral of various health and human services payments. The announced deferral period is July/August 2009. Assuming a near-term State budget adoption with no changes to the impacted health and human services programs, the deferred payments are due to be paid to the county in September. The specific program

identities and their corresponding deferral amounts are provided separately by the Departments of Health and Social and Employment Services.

Collectively, the deferral of State payments could result in an estimated 2-month General Fund revenue reduction of \$9 to 10 million to the county treasury. The county treasury has sufficient cash liquidity to meet the expected revenue reduction arising from deferred State payments. This capability is largely due to the use of the TRAN borrowing of \$55 million.

II. ISSUANCE OF REGISTERED WARRANTS (IOU'S)

Without budgetary authority, various State payments cannot be made. Consequently, the State Controller began the issuance of Registered Warrants, also known as IOU's on July 2, 2009. As is the case with deferred payments, the majority of State IOU's destined for counties pertain to the health and human services programs. At this time, the Treasurer has not been advised of any State IOU's that may be issued for Highway Users Tax payments.

The characteristics of the IOU's are:

- Appear similar to regular State checks with the additional script indicating the warrants are registered and cannot be deposited until October 2, 2009 or after that date.
- Interest will be paid to the presenter at the annualized rate of 3.75%.
- The Securities and Exchange Commission has determined the warrants are a municipal security and can be sold in the secondary market. Further, the Municipal Securities Rulemaking Board (MSRB) will regulate and designate acceptable entities to engage in secondary market activity.

The County's corresponding bank – Bank of America formally notified the Treasurer they will not accept Registered Warrants for depository credit after July 10, 2009.

Since most State payments to the county physically occur at a Sacramento Bank of America branch lockbox, the bank has agreed to forward via Federal Express all State Registered Warrants to the Monterey County Treasurer as soon as they are received by the bank (after July 10). The Treasurer intends to log the warrants, coordinate with the Auditor-Controller in establishing an account receivable system, develop certain security procedures and retain them until they can be redeemed – hopefully in October. The overarching concern is the stated redemption date on the warrants “... **on or after October 2, 2009**”. The uncertainty of the actual redemption date results in the county not receiving payment for programs funded by alternative sources (eg. TRAN) for an extended period, possibly into a later fiscal year.

The Treasurer does not plan to access the secondary market to redeem the State warrants as this will likely involve a sale of the warrants at a significant discount (loss) to full

value. However, if a market is identified that will pay full value upon presentment of the warrant, the Treasurer will consider early redemption.

As of July 10, 2009 the Treasurer received a total of \$193,704 from 9 Registered Warrants. Those warrants were credited to the county by Bank of America. Subsequent warrants will not receive credit. Should the State continue to issue Registered Warrants, the estimated monthly amount for county programs is \$0.7 million. The Treasurer has sufficient cash liquidity to cover this estimated cash shortfall for the next 4-5 months. The uncertain end-time for cash coverage reflects the unknown impact of the final State budget on county programs and the availability of alternative county funding sources. In addition, the County's short term borrowing (TRAN) must be 50% repaid by the end of 2009. This will substantially reduce the county's ability to provide cash should the State budget crisis persist for several more months.

III OTHER PUBLIC AGENCY ISSUES

The combination of the economic downturn and the State budget crisis has impacted all other public agencies, including those who are depositors (schools and special districts) and non-depositors (cities) in the county treasury. Consequently, those public entities are developing budgetary mitigations as well as cash flow augmentation plans. Historically, the county's cash flow plan involved a short term borrowing program using Tax and Revenue Anticipation Notes (TRAN) which is a one-year note payable in two increments during the fiscal year. This year the county borrowed \$55 million.

Other public agencies have access to TRAN programs. This year, four Monterey County school districts issued a TRAN. However, there are 22 districts that did not issue a TRAN. This may be a result of access to other internal borrowing sources, inability to access the TRAN market or simply not demonstrating a financial need. The same is true for the cities in Monterey County. Given the current economic situation and the deferral of State payments, the Treasurer believes all public entities in the county are experiencing fiscal and cash flow stress. The nexus with the county treasury is that all public agencies have legal authority under Article 16 of the State Constitution to request temporary loans from the county treasury. This is accomplished by an authorizing resolution from a governing body, approvals from the county Auditor-Controller as to compliance and the county Treasurer as to cash availability in the treasury. The Board of Supervisors has final authority to approve or deny the requested loan. Repayment of these loans is ensured by withholding property tax allocations by the Auditor-Controller.

For the past many years, several special districts (primarily fire protection districts) have annually engaged in temporary loans from the county treasury. The annual total of such loans has averaged around \$6 million. This year, there may be more public agencies opting to request cash flow funding from the county treasury. Specifically, the City of Pacific Grove has contacted the Auditor-Controller and Treasurer to begin preparation for a temporary loan. While these loans are permissible and secure as to repayment, there is a question about threshold tolerance given the State crisis. If all eligible cities and

districts requested a temporary loan from the treasury, there would be no available funds for routine expenses. Thus, a legal question of invoking limits on approval of temporary loans must be addressed.

Another potential impact on the treasury is from non-general fund county departments. The Road Fund is a particular concern. The State has indicated the possibility of severely reducing Highway Users Tax (Gas Tax) allocations and also reducing Prop. 42 funding. While these funds are not a part of the Registered Warrant process, they do represent a potential major revenue reduction that will require budgetary mitigation action by the Board of Supervisors. The Highway Users Tax is currently estimated at \$800,000 per month. It should be noted the county TRAN is a general fund cash program. Therefore, it cannot be used to supplant non-general fund shortfalls such as the Highway users Tax.

CONCLUSION

At the time of this report, the State budget status is uncertain. The State Controller began issuing Registered Warrant on July 2 and will continue to do so until State cash flow have improved. Beginning July 10 the county's bank will no longer accept Registered Warrants for depository credit. The Treasurer will secure the warrants and hold pending potential redemption on or after October 2. Based on the projected payment deferrals and IOU's from the State for county General Fund programs, the Treasurer believes there is sufficient cash to maintain program support for the next 4- 5 months. This is largely due to the proceeds from the county TRAN issue of \$55 million. Should the State not honor warrant deposits until much later than October 2, or if the budget stalemate continues the Treasurer would not have enough cash to continue funding General Fund programs and expenses.

Finally, the Treasurer could not provide any significant increase in temporary loans to other public agencies beyond the historical amount of \$5-6 million. The Treasurer recommends seeking an opinion on the authorities associated with these loans.