



RON GALPERIN
CONTROLLER

March 23, 2017

Honorable Members of the City Council

Subject: Judgment Obligation Bonds (Council File 16-1322)

In January of this year, you were asked to authorize the issuance of up to \$60 million in Judgment Obligation Bonds (JOBs) to reimburse the Reserve Fund for excess Liability Claims payouts. The Council authorized the CAO to move forward with the approval process on the understanding that a final Council approval would be needed prior to issuance. For the reasons outlined below, we are recommending that the City NOT proceed with the JOB at this time.

Under the terms of the proposed JOB, the City would borrow up to \$60 million to repay \$55 million in advances from the Reserve Fund to cover the liability payouts, with up to an additional \$5 million set aside for issuance costs. The stated goal of issuing the JOB was to maintain the Reserve Fund balance at or above the City's 5% policy threshold, and to provide flexibility for any unanticipated costs that may occur as we enter into the next fiscal year. As structured, the JOB would obligate the City to 10 years of debt service payments of approximately \$8 million annually. The JOB will be financed at a rate currently estimated at 5.5% (well over the 1-1.5% currently earned by the City Treasury pool where the funds will be deposited), which would require the City to pay approximately \$20 million in interest over the 10 year term of the bond.

When the CAO formally proposed the JOB, the City was facing a potential \$245 million deficit in the current year operating budget. However, the City's projected fiscal year-end deficit now stands at \$38 million, as detailed in my Office's March 1 Revenue Forecast and the CAO's Midyear Financial Status Report.

Today, the Reserve Fund totals \$278 million, 4.98% of the 2016-17 Adopted General Fund Budget – \$1.1 million below our 5% threshold. However, City departments will revert unspent funds at the end of the fiscal year and, assuming no further transfers out of the Reserve Fund, we conservatively project to finish the fiscal year with a Reserve Fund balance of \$316 million or 5.66% of the Adopted General Fund Budget.

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Once the new fiscal year begins and the Council-approved reappropriations are completed, the City is projected to start 2017-18 with \$289 million (or 5.2%) in the Reserve Fund. While the Reserve Fund balance for July 1, 2017 would be lower than the July 1, 2016 balance, it would still remain above the 5% policy. In addition to the Reserve Fund, the City currently has a balance of \$94 million in the Budget Stabilization Fund (BSF).

Given the improvement in the City's fiscal outlook, it no longer appears that issuing a Judgment Obligation Bond is necessary to maintain compliance with the 5% Reserve Fund policy. I believe that debt financing of liability claims should only be used in extraordinary circumstances and in times of great need. This year does not meet those criteria, and the City should live within its means instead of borrowing unnecessarily.

We understand that the current fiscal situation is challenging, and next year will certainly present even more challenges. Every department in the City will be pushed to continue delivering excellent service with fewer resources, no matter what the Council decides regarding the JOB. However, the City's leadership has consistently demonstrated strong fiscal policy since the Great Recession, through which we have grown our Reserve Fund and avoided short term solutions to long term problems.

We strongly encourage you to once again make the fiscally responsible choice, rather than committing the City to spending \$20 million in interest over the next 10 years for a one-time gain of \$55 million in 2017.

Sincerely,

A handwritten signature in black ink, appearing to read 'Ron Galperin', with a stylized flourish at the end.

RON GALPERIN
City Controller

cc: Honorable Eric Garcetti, Mayor
Richard H. Llewellyn, Jr., Interim City Administrative Officer
Sharon Tso, Chief Legislative Analyst