

Texas Public Finance Authority

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Kimberly K. Edwards
Executive Director



Post Office Box 12906
Austin, Texas 78711-2047
Telephone: (512) 463-5544

300 West 15th Street, Suite 411
Austin, Texas 78701
Telefacsimile: (512) 463-5501

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Opinion Committee

The Honorable John Cornyn
Attorney General of the State of Texas
Price Daniel Sr. State Office Building
Austin, TX 78701

RE: Request for Opinion concerning the application of Texas Government Code,
chapter 551 to actions required to issue and sell bonds

Dear General Cornyn,

The Texas Public Finance Authority ("Authority"), established by Texas Civil Statutes art. 601d, as a public authority and body public and corporate, is charged with the responsibility to issue and sell general obligation and revenue bonds and other obligations for certain state agencies and institutions of higher education. The Authority is also an "issuer" as defined in and for the purposes of Texas Civil Statutes art. 717q ("Article 717q"), which governs the issuance of bonds and other obligations.

Section 3 of Article 717q requires the governing body of an issuer to adopt an ordinance, order, or resolution authorizing the sale of bonds which establishes the terms, conditions, and covenants of the bonds, the maximum principal amount, maximum interest rates, payment dates, price, and manner of sale, either public (competitive sale) or private (negotiated sale). Section 3 also authorizes a governing body to designate one or more officers or employees to act on its behalf in selling bonds and establishing the dates, interest rates, maturities, prices, payment periods and other terms and conditions of the bonds as may be specified in and in accordance with the issuer's resolution, ordinance or order. This delegation of authority to price and sell bonds is particularly useful in negotiated or private sales of bonds.

The Authority's overriding goal in issuing bonds is to ensure that state debt is incurred at the lowest possible borrowing cost. To achieve this goal, the Authority's governing Board of Directors ("Board") may determine to sell bonds through a negotiated sale. In general, negotiated sales are chosen when it is determined that a more extensive and organized marketing effort is needed to obtain attractive interest rates, if an issue is interest rate sensitive (such as a refinancing) or if financial markets are volatile. One of the greatest benefits of a negotiated sale is that after the Board has established the general parameters for the pricing and other terms and conditions of the bonds in the bond resolution, which it adopts in a public meeting, the exact, technical features of the bonds can be established through negotiations between the issuer and the underwriter to maximize investor demand on the day of pricing and thus lower interest rates.

In a competitive sale, the date and time of sale, the structure and all features of the bonds are determined weeks in advance of the sale date in order to provide sufficient notice to potential bidders. The bids are opened in a public meeting. As soon as the interest rates shown in the bids are verified and compliance with all mandatory requirements of the bid is confirmed, the bonds are sold by the Authority accepting the bid with the lowest true interest cost.

For negotiated sales, in accordance with Section 3 of Article 717q, the Board may appoint one or more of its officers or employees to serve as a pricing committee to negotiate the final terms and conditions of the bond sale within the parameters established in the bond resolution and complete the sale by signing a bond purchase contract. It is not clear, however, whether such actions taken by a pricing committee composed of two or more but less than a quorum of Board members constitutes a "meeting" subject to the Texas open meetings act, Texas Government Code ch. 551 ("Act"). Additionally, it is unclear from the Act and prior interpretations thereof whether the Act prohibits holding open meetings outside the State. Because the issuer's effectiveness in pre-sale negotiations on price and timely response to offers and counter offers requires the issuer to be in touch with the market, bond pricings are typically conducted on the premises of the underwriter's trading desk.

The specific actions involved in a negotiated bond pricing and sale along with discussion of prior Attorneys' General opinions which may relate to these issues are more particularly set forth below.

The Authority respectfully requests your formal opinion on the following issues:

1. Whether a bond pricing attended by less than a quorum of the Board of the Authority in accordance with the delegation of authority authorized in Article 717q, section 3, constitutes a "meeting" under the Act?
2. If so, may the bond pricing be conducted outside the State?

The Authority requires clarification on these issues as it has been suggested that a designated pricing committee acting under Article 717q, Section 3 is a subcommittee of the Board. Open meeting requirements for subcommittees of governing bodies are not specifically addressed in the Act, but prior Attorney General opinions have determined that subcommittees may themselves be subject to the Act. See Op. Attorney General Nos. H-3 (1973) and H-238 (1974), which reasoned that committees developing recommendations in meetings closed to the public posed a danger that the full board could become a rubber-stamp of the committees, depriving the public of access to the actual decision making process. Other opinions have explained that a committee which meets to discuss any public business or public policy over which it has supervision or control is subject to open meetings requirements. (See Ops. Atty. Gen. Nos. H-772, 1976 and JM-1072.)

The activities required of a pricing committee do not appear to come within either of these two categories. First, the pricing committee acts only after the full Board has deliberated the material terms of a bond issue in an open meeting and adopted a resolution governing the sale. Thus, a pricing committee's activities do not present the potential harm to be avoided under the holding in Op. Atty. Gen. H-3 (1973) of a "rubber-stamping" process. Secondly, the activities of the pricing committee must be carried out only upon and within the limits of the Board's delegation, which occurs in an open meeting. Although the pricing committee exercises some discretion with respect to fixing the final terms of the sale, the discretion is limited to action within the provisions of the bond resolution already adopted by the Board.

The specific steps of a negotiated sale and the pricing process as implemented by the Authority may best illustrate this; in summary, they are the following:

1. As soon as possible following the Board's decision to use a negotiated method of sale, either at the same open meeting or the next open meeting, the Board also selects an underwriting syndicate, composed of two or more qualified investment banking firms, and designates one of the syndicate members to be the senior manager. In addition to serving as the representative of the syndicate in negotiating the sale and signing the bond purchase contract, the senior manager's duties include helping to structure the bond issue, keeping the order book, making allocations, and assessing and paying the syndicate's expenses.
2. Immediately after the senior manager is designated, the Authority's staff and its financial adviser, often in conjunction with the senior manager, prepare the preliminary bond structure which sets out a desired principal maturity schedule, the use of serial or term bonds, call provisions, and expected issuance costs and interest rates. The recommended structure is reflected in the bond resolution, which is considered and adopted by the Board in open meeting. If a pricing committee is to be used, the tentative day of pricing is scheduled and members of

the committee are notified. It should be noted that the pricing date for interest rate sensitive transactions, such as refinancings, can often be established only one or two days prior to the sale to achieve the savings threshold established by the Board.

3. On or before the day before the pricing, the Authority's staff and financial adviser begin discussion of the bond structure and sale, including matters such as the anticipated market or demand for the bonds, anticipated interest rates, yields, call features, redemption provisions, priority of orders, and underwriters' fees and liabilities.

4. On the day of the pricing, following a final discussion of the initial interest rate scale between the Authority's representatives and the senior underwriter, the senior underwriter recommends terms and conditions of the bond structure and sale at which the bonds should be offered initially.

5. After an initial offering scale is approved by the Authority, an initial order period of two or three hours begins, during which members of the underwriting syndicate place investors' orders. The initial order period shows investor interest in the issue, and the orders are monitored closely by the Authority and the senior underwriter.

6. If the initial orders show there is little demand for the bonds, the bonds may have to be repriced or restructured to attract more investors. If there is more demand than supply, the bonds might be repriced to lower the yield. Repricing involves changing one or more of the following factors: coupon, yield, call features, maturity amount, or sales concession.

For example, one of the largest determinates of a bond's price (interest rate) is its call feature. Bonds that can not be called prior to maturity bear an interest rate that is 05 to 20 basis points lower than "callable bonds" of a similar maturity. The exact difference in price, and whether the issuer deems it worthwhile to pay that price differential, depends on the interest rate environment, investor demand, and the particular facts of the project being financed (i.e., how likely is it that the issuer will want/need to call the bonds prior to maturity). The bond resolution, which is adopted by the Board in an open meeting prior to the bond sale, specifies the general parameters of the call feature: whether all or a portion of the bonds will be callable, and the earliest possible date on which they can be called. On the day of pricing, the underwriter and issuer negotiate the exact call features based on investor demand on that day: which bonds will be callable, the exact call date, and

the call price. Since the “value” of these call features change on any given day, the negotiated sale process allows the issuer to obtain the best deal on that day.

7. Following final agreed adjustments to the pricing, the senior underwriter makes an offer to purchase the bonds upon the agreed terms. The persons designated by the Board as having the authority to do so may complete the sale by orally accepting the underwriter’s offer. A written bond purchase contract is signed subsequently, preferably within 24 hours following the oral award.

Even though market information and anticipated demand for the bonds has been analyzed, it is not possible to determine exactly how a bond issue will sell until the bonds are in the market. To successfully price its bonds, the issuer’s pricing committee must have direct access to market information generally, and information of the amount and type of orders placed during the initial order period. It must also be in a position to ask questions of the underwriter, quickly analyze the need to reprice or adjust yields, or to negotiate other adjustments in the pricing such as increasing or decreasing the underwriters’ commission or fees. Although the ability to negotiate and renegotiate is extremely important to ensuring that the Authority is borrowing for the State at the lowest possible cost, it does not require the pricing committee to deliberate policy matters or exercise discretionary policy decision-making. The pricing committee’s job is fairly technical and ministerial in carrying out the policy direction and decisions of the full Board as set out in the bond resolution. The public is in no way denied access to a decision making process.

For these reasons, we believe that the question of whether a bond pricing by a pricing committee constitutes a meeting under the Act has not previously been determined.

The Authority has been advised that if the Board delegated the authority to price and sell bonds to a pricing committee consisting of only one Board member, the bond pricing and sale actions would clearly not raise a question of the applicability of the Act. The Authority is further informed that other similarly situated issuers routinely delegate authority to price and sell bonds only to staff, staff actions and deliberations are not subject to Act. Also, in an effort to try to achieve the best financial results for the State on a recent refinancing issue, the Authority has resorted to the fail-safe procedure of posting daily or “evergreen” open meetings notices until the bond issue was sold. Although such technical compliance is possible, it is not a satisfactory long-term resolution because it is a form over substance, may overburden public administration, and provides questionable public benefit. The Authority understands that the same procedure has been used routinely by other issuers.

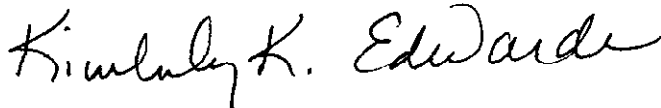
If it is determined that a bond pricing by a committee of two but less than four Board members does constitute a “meeting” under the Act, would it not be possible to conduct such “meeting” at the location where the purpose of the meeting may be most effectively accomplished? Negotiated

bond pricing frequently takes place at the location of the senior underwriter's trading desk. It is more likely than not that the trading desk is located at the firm's main office, which is often in New York City or other regional financial center. The presence of the pricing committee, particularly one composed of members of the Board, is advantageous for a number of reasons. It indicates to the underwriter the issuer's intent to be actively involved in the sale, allows the issuer to monitor the legitimacy of orders and underwriters' representations of investor demand, ensures meaningful negotiations, and guarantees that persons with the authority to act are available to respond to market conditions.

As previously reviewed, the policy considerations and the exercise of discretionary decision making with respect to a bond issue and sale are subjects of the Board's open meetings in advance of the actual pricing and sale. The technical decisions and negotiating that must take place at a pricing would not enlighten or benefit the public. Because of the specific activities that take place during a pricing session, we would respectfully suggest that the location of a pricing outside the State does not violate or offend the letter or the spirit of the Act.

Thank you so much for your consideration of these matters. If you have questions or require additional information, please call me at 463-5544.

Sincerely

A handwritten signature in cursive script that reads "Kimberly K. Edwards". The signature is written in black ink and is positioned above the typed name.

Kimberly K. Edwards
Executive Director