

HOW CERTIFICATES OF PARTICIPATION WORK FOR OREGON

What are Certificates of Participation or COP's?

COP's are tax-exempt government securities used to raise funds to improve and construct buildings or purchase equipment. COP's are used to finance capital costs related to construction or acquisition and may not be used to finance ongoing operating costs. COP's are sold to investors who like the good credit quality of Oregon. In return, the investors receive COP payments which include interest income that is exempt from federal and Oregon income tax. COP's are used very selectively in Oregon to implement projects essential to delivering public services.

How do COP's differ from general obligation bonds?

General obligation (GO) bonds are secured by the full faith and credit of the government issuing them. The government's taxing powers may ultimately be called upon to repay the bonds. In Oregon, general obligation bonds are authorized by amendments to the Oregon Constitution. COP's on the other hand, are not secured by the full faith and credit of the issuer. Instead, in Oregon the Legislature must approve the COP repayment amounts prior to each biennium for which payments are scheduled. In other words, the Legislature could deny a budget request for COP debt service. Should the State fail to make scheduled COP payments, the state may be denied use of the financed building(s) and equipment. Furthermore the ability of the State to obtain financing for future needs would be lost.

The COP program currently has a lower credit rating than the State's GO bond program.

<u>Debt Instrument</u>	<u>Ratings Summary</u>	
	<u>Rating Agency</u>	
	<u>Moody's</u>	<u>Standard & Poor's</u>
<i>General Obligation</i>	<i>Aa2</i>	<i>AA</i>
<i>COP</i>	<i>Aa3</i>	<i>AA-</i>

Oregon Supreme Court validated the COP authority.

On December 4, 1989, the Oregon Supreme Court dismissed a case challenging the constitutionality of the Oregon COP authority passed into law by the 1989 legislative session.

Oregon has strong controls on the use of COPs.

COP issuance and spending authority for related projects must be authorized by the legislature. Individual sales of COPs require approval by the DAS Director and the State Treasurer.

Oregon law and the COP program procedures provide a strong structure to process requests for financing projects by state agencies. The Department of Administrative Services (DAS) manages the COP Program as a central service function. It operates as part of the Budget and Management Division's Capital Investment Section. Centralized control assures that COPs are only used for projects approved by the Legislature and the Executive Branch.

COP Approval Process

Agency Request and Governor's Recommended Budget

Agencies identify all projects for which they seek COP financing. COP financing requests are evaluated in terms of the type of project and appropriateness of the use of COP financing. The requests are then considered within the context of the agency's total budget, source of funds for repayment and the Governor's policy and spending priorities. This review determines which requests are included in the Governor's recommended budget.

Legislative Approved Budget, "Bond Bill" and Capital Construction Bill

The project and financing requests are presented as part of each agency's budget. Authority to issue COPs related to approved projects must also be approved in the "bond bill." The "bond bill" refers to debt limit legislation required by ORS 286.525. Capital construction projects must be approved in the "capital construction bill." Capital construction projects are often financed using COPs. Approval of the bond bill and capital construction bill is usually scheduled late in the session to give legislators the "big picture" view of the individual COP financings approved in agency budgets. It allows consideration of the financings within the context of the total COP, general obligation and revenue bond authority the Legislature has been requested to approve for the upcoming biennium.

Time of Sale and Thereafter

The express approval of both the State Treasurer and the DAS Director is required as part of the issuance of COPs to finance approved projects. This step provides a safeguard in the event circumstances have changed subsequent to budget approval.

- DAS and the program trustee monitor use of COP proceeds to ensure that they are used only for allowable purposes under State law and the Internal Revenue Code. Proceeds are invested during project implementation to maximize

earnings. DAS also assists agencies in developing budget requests to ensure that required debt service amounts are included in budgets. DAS facilitates payment of COP debt service. The DAS Capital Investment Section works with the Treasury to make all necessary disclosures under Security and Exchange Commission regulations, and with the State Controller's Division for financial reporting. DAS also works with agencies to ensure adequate property loss insurance on the assets pledged.

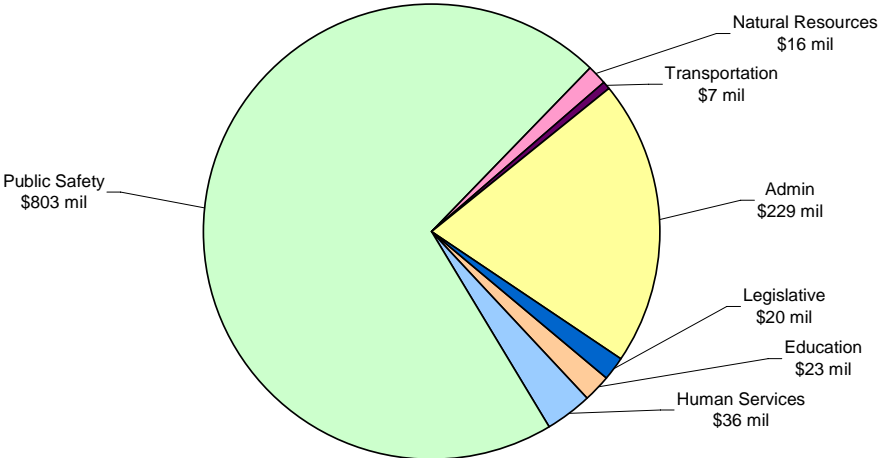
Oregon has been very selective in its use of COPs.

During the period from 1990 through December 31, 2007, Oregon has sold \$1,689.2 million new issue COPs. The proceeds have for the most part financed projects for four core purposes. 62.0% of COP funds have been used for *public safety*, 6.9% for *higher education*, 1.4% for *transportation*, and 29.7% for *central services* projects. A large share of the financing for central services projects was used to remodel and construct office space in Salem and Portland. Those projects include the Public Service Building, the Public Utility Commission Building, Capitol renovation, the Forestry complex on State Street and the Human Resource Building in Salem.

How many COPs are currently outstanding?

As of December 31, 2007, a total of \$1,135 million of COP's issued under ORS 283.085 were outstanding. Below is a chart that show the outstanding COP's at December 31, 2007 by budget area.

Certificates of Participation by Budget Category



How many additional COPs can be issued?

Although there is no statutory limit on outstanding COPs, there is a practical limit based on the State's ability to repay this and other debt. The State Debt Policy Advisory Commission (SDPAC) made recommendations regarding prudent levels for future debt issuance in its January 14, 2008 report. COPs are included in a category referred to as **General Fund supported** debt. In addition to COPs, General Fund supported debt includes Article XI-G bonds for Higher Education and Community Colleges, pollution control bonds and several other programs.

The SDPAC recommended issuing no more than \$1 billion in General Fund supported debt (all programs) per biennium through fiscal year 2013. This recommendation is subject to change should the State's revenue forecast change.

Some advantages of Using COPs

Financing spreads the capital costs of projects over several years. The State is able to take advantage of unique opportunities or relatively lower costs during times of rising prices. Often the State can accommodate debt service from current resources current without significant impacts on service delivery in other areas. This might not be possible if the State was required to fund major capital projects from current resources. In effect, the financing leverages general fund revenues to acquire the resources needed to implement cost effective or mandated projects today.

Some of the capital costs of providing an asset such as a prison are spread to future public beneficiaries of the asset. This matches public user benefits to public user charges over time.

As with Oregon general obligation and revenue bonds, the interest received by COP investors is exempt from both federal and Oregon income taxes. Therefore, the State's interest expense is lower than it would be using conventional financings.

The central management of the COP Program provides several strengths. Central management helps assure the financings are consistent with approved budgets. Using financing documents that include uniform provisions that protect the state's best interests also serves state agencies that are unfamiliar with the public finance sector. The COP approval and issuance work is a team effort. The user agency, budget analysts, assistant attorney generals, Treasury, bond counsel, legislative fiscal officers, and others work together to achieve cost effective financing terms for projects approved by the legislature.

Additional information regarding Oregon COP's can be obtained from Jack Kenny, Finance Manager, Department of Administrative Services, (503) 378-3107