Bond Business Fueled Battle Over Lungren

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SACRAMENTO — The hardball politics surrounding the confirmation battle over Gov. George Deukmejian's nominee for state treasurer can be reduced to one word: money.

Under the regime of the "Big Daddy" of the California Legislature — the late state treasurer and Assembly Speaker Jesse Unruh — the musty, ministerial, low-profile office of treasurer assumed staggering financial and political importance.

As treasurer, Unruh demonstrated unexpected wizardry on Wall Street, impressing the financial community and ultimately extracting from it healthy campaign contributions — the *quid pro quo*, some critics say, for favorable treatment by the many state agencies under Unruh's control or influence.

Ironically, the liberal Democrat Unruh invigorated the office that the Republican governor now must fill, and as a result, the new treasurer could be catapulted to significant political power.

That nominee, Rep. Dan Lungren, a Long Beach Republican, is fighting the battle of his political career. After weeks of combative hearings, the Democrat-controlled Legislature is scheduled to vote on Lungren's nomination today.

The pivotal factor, according to capital observers, is the bond business.

While the legislators battle Deukmejian over Lungren, another fight looms in the wings over the governor's plan to issue unprecedented billions of dollars in bonds to finance major capital projects such as schools, highways and prisons. Deukmejian proposed at least $4.7 billion in state bonds for the June and November ballots. Legislators have introduced bills to authorize more than $13.7 billion in bonds, including much of the governor's plan.

Just offstage are thousands of under-

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– work that often is doled out with no competitive bidding and conducted out of public sight.

But the esoteric, lucrative bond law business is being drawn out of the shadows — somewhat to the consternation of its private practitioners in the financial and legal communities. They prefer to work quietly.

"After voter approval, bond measures nearly always sink from public view," reported the Senate Office of Research.

To transform the voters' will into public funds, the treasurer must hire bond attorneys, underwriters, printers and other specialists.

In 1987, the researchers say, private businesses and professionals received about $56 million for their part in helping the state issue $3.7 billion in bonds.

But 1987 was an off year compared to 1986, when the treasurer assigned about $120 million worth of business to technicians and lawyers, who prepared $7.5 billion in bonds, the report says.

The treasurer's decisions often are made without any public bid, rationale, explanation or appeal.

"The selection rides on the treasurer's subjective judgment . . . in sharp contrast to the sometimes tedious public procedures governing almost all other state spending," the Senate researchers say.

Among the army of lawyers angling for state bond work, none can compare with San Francisco's Orrick, Herrington & Sutcliffe — the state of California's premier bond counsel for nearly a century.

The firm's plush Sacramento offices offer some testament to its power in the bond business. Two large, glassed-in conference rooms flank the 12th-floor entry in Orrick's swank office building. The suite is furnished with marble-inlaid conference tables and decorated in a pleasant, contemporary burgundy and mauve color scheme. Exotic fresh flowers grace the waiting room. The offices offer an unfettered view of the Capitol dome.

With other satellite offices in New York and Los Angeles, Orrick employs about 250 lawyers, including 65 in its public finance department. In that department, 60 lawyers are bond specialists. The firm also employs two full-time, non-lawyer lobbyists in Sacramento. Ten years ago, fewer than a dozen lawyers were in Orrick's public finance division.

Orrick contributed heavily to Jesse Unruh's fabled campaign fund — donating $30,000 from 1983 to 1986, according to a 1986 report in the Los Angeles Times.

Although big investment banking firms such as Merrill Lynch Pierce Fenner & Smith and Paine Webber made the largest contributions — more than $50,000 each — Orrick and other large bond law firms were major players in the treasurer's campaign war chest from 1983 to 1986, the Times reported. Los Angeles' O'Melveny & Meyers trailed Orrick with $19,500, followed by Los Angeles' Buchalter, Nemer, Fields, Christie & Younger with $16,850, and the defunct national firm Finley, Kumble, Wagner, Heine, Underberg, Manley & Casey with $10,750.

Former California Attorney General Evelle Younger, whose firm, Buchalter, Nemer, entered the state bond business in 1983 and is now one of its major players, did not apologize for his firm's contributions to Unruh.

"I don't think people hire lawyers who they think are stupid," Younger says. "If we didn't [contribute], then we would be stupid with a capital 'S.' "

The late treasurer insisted that there was no conflict of interest for him to handle bond decisions affecting campaign contributors.

"I can't disqualify myself from everything that I might touch in this business anymore," Unruh said. "Otherwise, I couldn't have a personal bank, I couldn't have a personal broker. I probably might run into conflicts where I couldn't have an attorney."

And, the late treasurer told The Wall Street Journal in a now-famous admission: "Probably as long as all things are equal and all firms are equally capable, we do tend to go with them if they are friends."

ROBERT P. FEYER: "We are selected for our skills . . . not political contributions. We are not a political firm," said the Orrick, Herrington & Sutcliffe partner.

Unruh insisted that his power was not "totally discretionary" and that he did not control all the bond-issuing authorities.

Even his critics say Unruh was a wise and prudent, if sometimes dictatorial, investor for the state, bringing the state's bond rating up to AAA and, according to his office, earning $1.3 billion in 1985 alone for the various funds controlled by the treasurer's office. That amount equals 87 percent of the total earnings of all 25 of Unruh's predecessors.

Bond specialist Robert Feyer, an Orrick partner who maintains offices in San Francisco and Sacramento, bristles at the suggestion that campaign contributions might influence the selection of bond counsel. "That is entirely unfounded," he says flatly. "It is my very strong belief and the firm's belief that we are selected for our skills and that [the selection] is entirely due to the quality of our work and our ability to provide excellent service to agencies — not political contributions. We are not a political firm. We don't have partners who are heavyweights in either party . . . If political contributions were the measure, you would see a lot more [firms] contributing."

Orrick contributed to Unruh "because we were asked," Feyer says. "Unruh made it known that everyone had to contribute to be on the playing field."

Although campaign contribution figures are readily available in central state records, no centralized state figures are kept on such bond lawyer fees.

Assistant State Treasurer Kenneth Cramer says that pinpointing the fees of bond counsel is difficult because each state agency or fiscal authority handling a particular bond issue arranges all the administrative details.

"Unlike many things that are billed, bond counsel is paid out of the proceeds [of the bond]," Cramer says. "We keep a lot of records with respect to bond sales, but not on that."

Orrick collects 7 cents for every $1,000 of face value for general obligation bonds. These instruments are referred to in the bond community as "pure vanilla" or "simple vanilla" bonds, which comprise relatively straightforward transactions and are backed by the full faith and credit of the state.

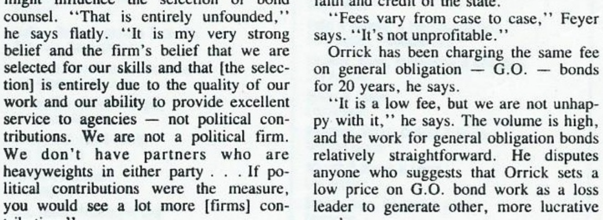
"Fees vary from case to case," Feyer says. "It's not unprofitable."

Orrick has been charging the same fee on general obligation — G.O. — bonds for 20 years, he says.

"It is a low fee, but we are not unhappy with it," he says. The volume is high, and the work for general obligation bonds relatively straightforward. He disputes anyone who suggests that Orrick sets a low price on G.O. bond work as a loss leader to generate other, more lucrative work.

If competitive bidding were used, the Senate researchers concluded, the cost probably would be higher for the same work.

"On the other hand, the visibility and access to information and people have value in other ways, and other firms are denied those advantages," the researchers say.



SHARON STANTON WHITE: The Jones, Hill, Hill & White partner predicts firms will demand fewer bond lawyers as a result of the Tax Reform Act of 1986.

"In most cases it's Orrick. They have the expertise, and their charges are reasonable."

State officials familiar with the bond business say the big money for private bond lawyers in recent years has been found in the so-called conduit bonds, revenue bonds issued, with the state as a "conduit," for the private construction of facilities such as hospitals and pollution control projects.

"There is more money in a conduit-type bond," Cramer says. "But there is also much more work involved."

Selection of bond counsel for the more lucrative revenue bonds is "much more variable" than the selection process for general obligation bonds, the Senate researchers concluded: "The treasurer has selected a firm to serve as bond counsel on a regular 'team' basis for each authority. These selections are made based on the treasurer's subjective judgment. There is no competitive bid, nor any public explanation for why a particular firm was picked."

The treasurer often takes the recommendation of the local districts involved in the financing, they say.

The fee for bond counsel on revenue bonds, the report notes, ranges from less than $50,000 to more than $100,000, depending on size and complexity.

In addition, the government entity pays fees for underwriter's counsel, which might cost $100,000 in a $100-million bond issue.

Deputy Attorney General Walter Wiesner, who works with private bond counsel and issues an opinion for the attorney general (which may or may not agree with the private counsel's opinion, sometimes necessitating court review), estimates that bond counsel make 50 cents to $1 per $1,000 on conduit bonds.

"It's a fair piece of change," says Wiesner, who has been doing the bond work in the attorney general's office almost singlehandedly for two decades. He now has help from Deputy Attorney General Corinne Murphy, who handles bond work three days a week.

Wiesner says the 7 cents per $1,000 on general obligation bonds is one of the lowest bond counsel fees in the nation. For firms like Orrick, he says, "it's a loss leader, but it means they have the reputation of working on major state issues" — in turn generating significant other bond business.

Feyer says Orrick's revenue-bond fees are charged on an hourly, not a percentage, basis, ranging from $25,000 to $150,000 depending on the complexity of the bond work required.

As a result of changes imposed by the Tax Reform Act of 1986 and the fact that many bonds are no longer tax-exempt, some bond lawyers see major changes ahead in their specialty — including layoffs, reassignments and reassessment.

"There is no question that it's changing, with less work on conduit bonds and more work on state G.O. bonds," says Feyer. "In the long run, we see a shift in the market."

And yet, despite tax code changes that may make conduit/revenue-bond work less attractive, bond lawyers say the state's neglected schools, roads, prisons and other obsolete facilities need major repairs and construction, necessitating large bond issues.

Sharon Stanton White, a San Francisco bond lawyer with the firm of Jones, Hill, Hill & White, and immediate past president of the National Association of Bond Lawyers, says that the coming months may see "a modest decrease" in the number of bond lawyers because of the tax reforms. But, she added, the act also made bond work "more complex," prompting the need for competent, specialized legal advice.

At Orrick, Feyer says the changes wrought by the tax act have not prompted any reductions at that firm: "In California, we've kind of plateaued our staff — we have not cut back, but we have not grown substantially."

Bond lawyer Michael McCall, the principal bond lawyer with the large Sacramento firm of Weintraub, Hardy, Genshlea, Erich & Brown, says his firm plans to add two bond lawyers — even as other firms reportedly are cutting back or reassigning bond lawyers.

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