



PENSION OBLIGATION BONDS

A TOOL FOR CONSIDERATION FOR MANAGING THE CITY'S UNFUNDED LIABILITY





BACKGROUND

CITY'S PENSION PROFILE

CITY HAS A VERY STRONG CREDIT RATING

BUT PENSION LIABILITY IS A CONCERN

S&P's Rating Categories

AAA

AA+

AA

AA-

A+

A

A-

BBB+

BBB

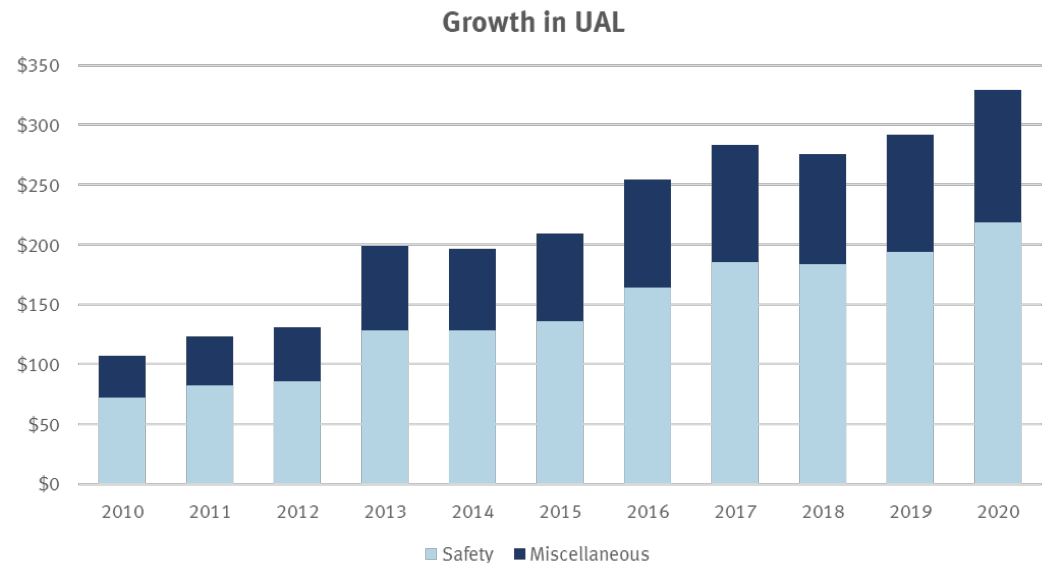
BBB-

- Credit rating agencies provide an independent appraisal of the credit quality of government agencies
- The City has an issuer credit rating from Standard & Poor's ("S&P") of 'AA+'
 - Reflects an upgrade of TWO NOTCHES in September 2021
 - S&P labeled the City '**very strong**' (its highest qualitative category) in the areas of Financial Management, Liquidity, Budgetary Flexibility and Debt & Contingent Liabilities and '**strong**' (second highest category) related to the area's Economy and the City's Budgetary Performance
- S&P noted, however, the City's large pension liability as an area of some concern and a constraint on further upgrade
- Potential enhancement to the City's credit rating when financing the upcoming Civic Center/Police Facility project

COMPONENTS OF THE CITY'S PENSION COSTS

OF PRIMARY CONCERN IS THE UAL

- Each year, three amounts are paid to CalPERS; for FY 2023, these are:
 - City normal cost = \$13.1 million
 - Employee normal cost = \$4.7 million
 - Unfunded Accrued Liability (“UAL”) = \$27.6 million
- The primary cost driver is the UAL, which has increased >300% since 2010
 - Represents how much the City needs to have in the future when people actually retire
 - Amortized over time at a discount rate (proxy for CalPERS anticipated earnings rate)



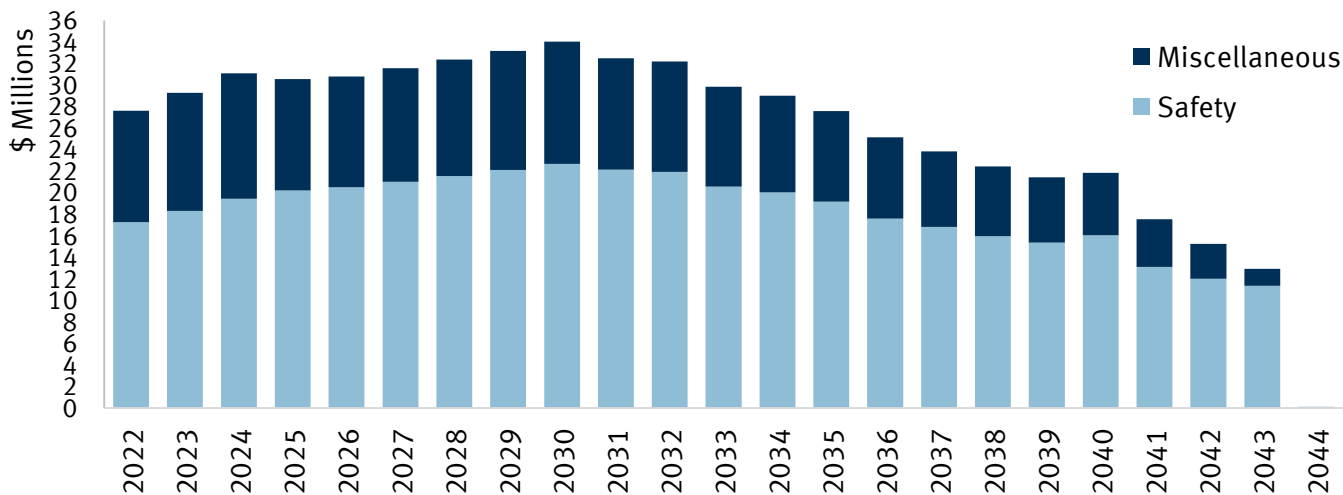
FUNDED STATUS OVERVIEW

UAL EXCEEDS \$300 MILLION AT MOST RECENT VALUATION

UAL Calculation Based on CalPERS 6/30/2020 Valuation

		Miscellaneous	Safety	Total
A	Present Value of Projected Benefits	\$394,410,411	\$643,919,219	\$1,038,329,630
B	Entry Age Normal Accrued Liability	\$351,307,306	\$581,960,501	\$933,267,807
C	Market Value of Assets (MVA)	\$240,644,136	\$363,308,360	\$603,952,496
D	Unfunded Accrued Liability (UAL)	B - C	\$218,652,141	\$329,315,311
E	Funded Ratio	C / B	62.4%	64.7%

Projected Combined UAL Payments



Note: Does not include the net impact from 21.3% return in 2021 and change to 6.8% discount rate. Does not consider funds held in Section 115 Trust.



PENSION FINANCING

MANAGING PENSION EXPENSES



PENSION OBLIGATION BONDS

A MORE FREQUENT OCCURRENCE FOR CALIFORNIA LOCAL GOVERNMENT AGENCIES

- Over the past 3 years CA cities, counties and special districts have sold \$6.9 billion of pension bonds, ranging in size from \$5 million to \$720 million, and rated between 'AAA' and 'BBB+'
 - For City's rating category and size, the cost of borrowing has ranged from 2.20% to 3.72%

Recently Issued California POB Issues Greater than \$40 Million

Sale Date	Issuer	Structure	Amount (\$M)	Final Maturity	All-In TIC
AAA Ratings					
12/14/21	Poway	POBs	\$43.83	2048	2.82%
09/02/21	Santa Cruz County	POBs	\$124.20	2047	2.47%
04/28/21	Manhattan Beach	POBs	\$91.28	2043	2.75%
10/27/20	Arcadia	POBs	\$90.00	2040	2.70%
02/05/20	Pasadena	POBs	\$131.81	2038	3.06%
08/22/19	Glendora	POBs	\$64.42	2044	2.85%
AA+/AA Ratings					
09/29/21	Corona	POBs	\$276.71	2034	2.20%
08/26/21	Santa Ana	POBs	\$425.83	2044	2.82%
08/17/21	Buena Park	POBs	\$96.39	2043	2.39%
07/14/21	Covina	POBs	\$62.80	2046	2.64%
05/26/21	El Segundo	POBs	\$144.14	2040	2.59%
03/17/21	Huntington Beach	POBs	\$363.65	2044	2.94%
03/03/21	Orange	POBs	\$286.49	2044	2.75%
02/11/21	Chula Vista	POBs	\$350.03	2045	2.53%
02/09/21	Downey	POBs	\$113.59	2044	2.63%
07/01/21	Redondo Beach	LRBs	\$226.18	2049	2.82%
08/03/21	Whittier	POBs	\$133.90	2046	2.59%
02/02/21	Monterey Park	POBs	\$106.34	2043	2.67%
01/13/21	El Cajon	POBs	\$147.21	2043	2.84%
10/14/20	Torrance	LRBs	\$349.52	2043	3.45%
06/04/20	Riverside	POBs	\$432.17	2045	3.69%
05/12/20	Ontario	POBs	\$236.59	2050	3.72%
04/22/20	Riverside County	POBs	\$720.00	2038	3.53%

Recently Issued California POB Issues Greater than \$40 Million

Sale Date	Issuer	Structure	Amount (\$M)	Final Maturity	All-In TIC
AA- Ratings					
08/17/21	Commerce	POBs	\$27.88	2041	2.65%
11/19/20	Coachella	POBs	\$17.59	2035	2.99%
11/10/20	Gardena	POBs	\$101.49	2039	3.33%
09/17/20	Azusa	POBs	\$70.08	2040	3.18%
08/13/20	Pomona	POBs	\$219.89	2046	3.52%
06/10/20	Carson	POBs	\$108.02	2050	3.38%
06/02/20	Inglewood	POBs	\$101.62	2050	3.91%
09/24/19	Hawthorne	POBs	\$121.87	2049	3.61%
02/20/19	Baldwin Park	POBs	\$54.09	2044	4.29%
A+/A Ratings					
07/23/20	West Covina	LRBs	\$204.10	2044	3.72%
12/02/20	Ukiah	LRBs	\$49.88	2049	3.92%
06/09/20	El Monte	POBs	\$118.73	2050	3.71%
A- Rating					
05/27/20	Montebello	POBs	\$153.43	2045	4.02%
BBB+ Rating					
10/29/20	Placentia	LRBs	\$52.95	2045	4.25%

WHAT IS A PENSION OBLIGATION BOND

ESSENTIALLY A LOAN TO PAY OFF DEBT TO CALPERS

Unfunded Accrued Liability

- City owes \$329 million to CalPERS
- City pays the discount rate (7%, now 6.8%)
- Effective cost is an adjustable rate that increases when earnings targets aren't met
- New UAL can be added if CalPERS' assumptions change or future interest earnings are below the discount rate
- Final payment is 2045

Pension Obligation Bond

- City would owe \$329 million to investors
- City would pay 3%-3.5% (est.) on the bonds
- Bond rate is a fixed interest rate that does not change for the term of the bonds
- New UAL can be added if CalPERS' assumptions change or future interest earnings are below the discount rate
- City can modify to meet its objectives

STRUCTURING ALTERNATIVES

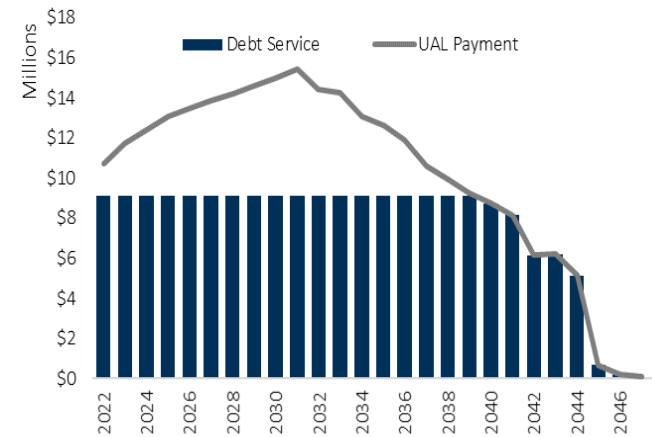
CITIES HAVE TAKEN VARIED APPROACHES

City of Whittier – 2021 Pension Obligation Bonds

UAL Funded: \$56.9 million | All-In TIC: 2.60%

Strategy - Consistent debt payment for easier budgetary control and financial planning

Whittier, facing a steep increase in its CalPERS payments, saw POBs as a way to level out its payment obligation. The modified level approach will allow the City to direct cash flow savings into reserves while maintaining level payments in most years and savings in every year.

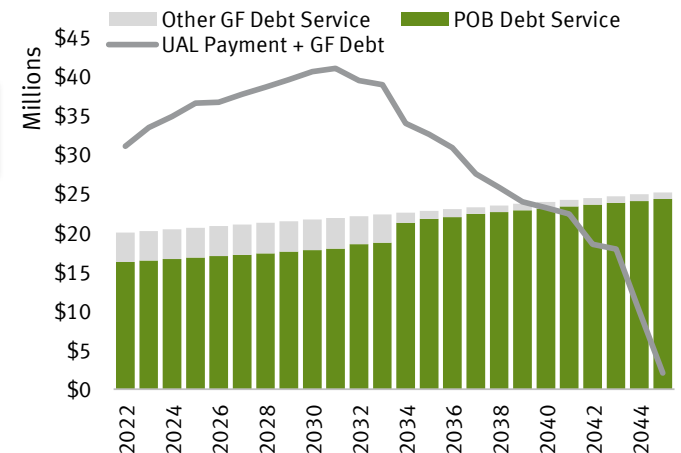


City of Chula Vista – 2021 Pension Obligation Bonds

UAL Funded: \$348.2 million | All-In TIC: 2.54%

Strategy - Building up reserves with cash flow savings

Chula Vista structured its POB to wrap around existing General Fund debt service and, in combination, sculpt an aggregate 1% escalating debt service obligation. A pension management policy was adopted to direct early years' savings towards bolstering reserves.



STRUCTURING ALTERNATIVES

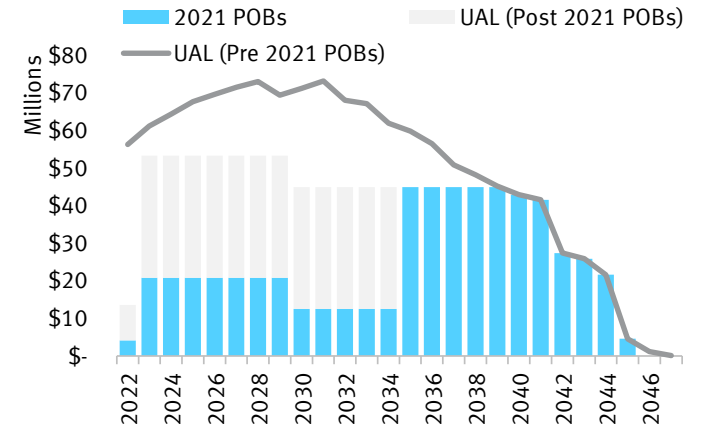
CITIES HAVE TAKEN VARIED APPROACHES

City of Santa Ana – 2021 Pension Obligation Bonds

UAL Funded: \$424.6 million | All-In TIC: 2.82%

Strategy – Staggered POB issuance; alleviate cash flow burden

Santa Ana wished to maintain level total pension payments over the next 10-years, then have them decline to a lower level structure. The POBs were sculpted in a way to create an all-in level structure in combination with the unfunded portion of the UAL.

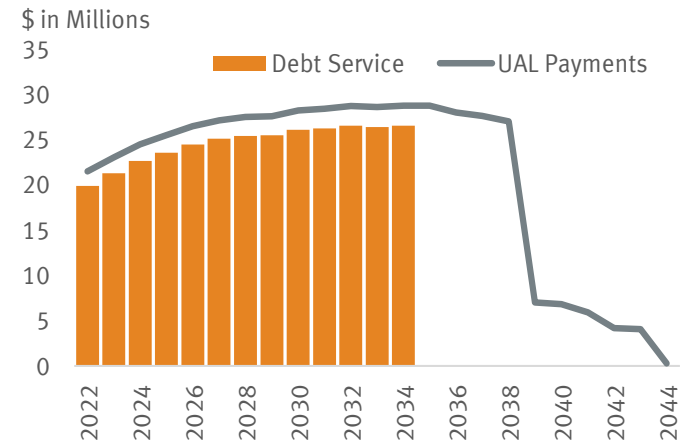


City of Corona – 2021 Pension Obligation Bonds

UAL Funded: \$275.6 million | All-In TIC: 2.23%

Strategy - Match current cash flow, and reduce debt payment period by 10 years to achieve higher savings

Corona sought to take its savings in the form of a shorter time period for repayment. This ‘accelerated’ approach has the city repaying its CalPERS liability 10 years earlier than otherwise scheduled.



ADVANTAGES OF PENSION BONDS

POTENTIAL FOR FASTER PAYOFF AND SUBSTANTIAL SAVINGS

Financially
Responsible

Proactively taking steps to get a handle on our pension expenses is the right thing to do

Historic Low
Interest Rates

Could reduce our cost of borrowing in half (or more)

Cash Flow Savings

We have an ability to sculpt the payment plan to our needs, either paying off sooner or capturing cash flow savings

Overall Savings

Could reduce our overall costs by 30% (+/-)

RISKS OF PENSION BONDS

RISKS INCLUDE EXTREME MARKET RETURNS AND SQUANDERED SAVINGS

Market Risk

If CalPERS' average investment return is less than the bond rate, then the pension bond would not result in savings to the City

Super-Funded Plan

If CalPERS over-performs, City could end up with its plans more than 100% funded

Locked In for 10 Years

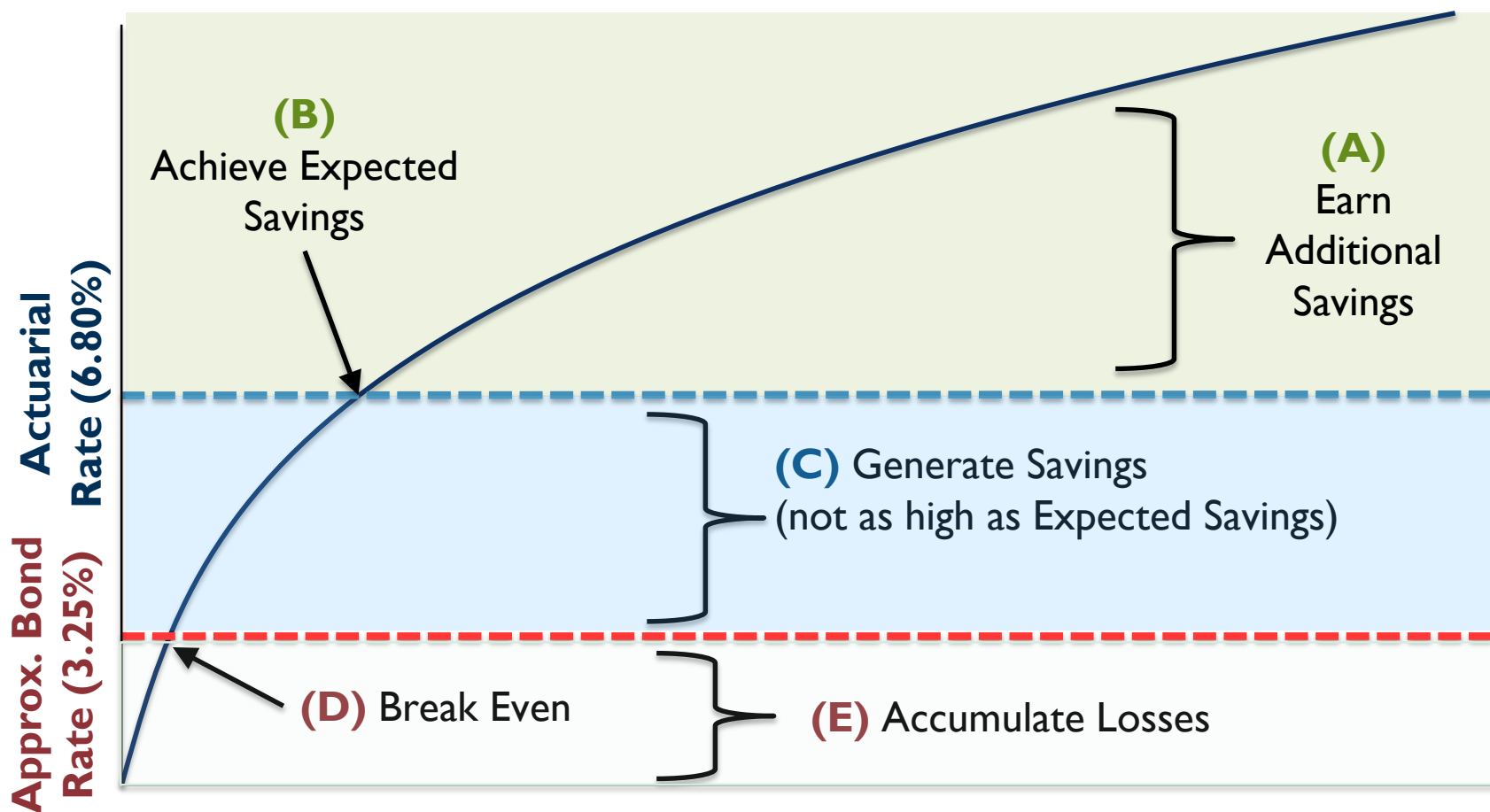
The bonds cannot be paid off for ten years; after the 10 year mark, the bonds can be refinanced or paid down

Squandered Savings

A future Council could take the savings and spend them on projects/services that don't enhance the City's financial position

PENSION "SAVINGS" OVERVIEW

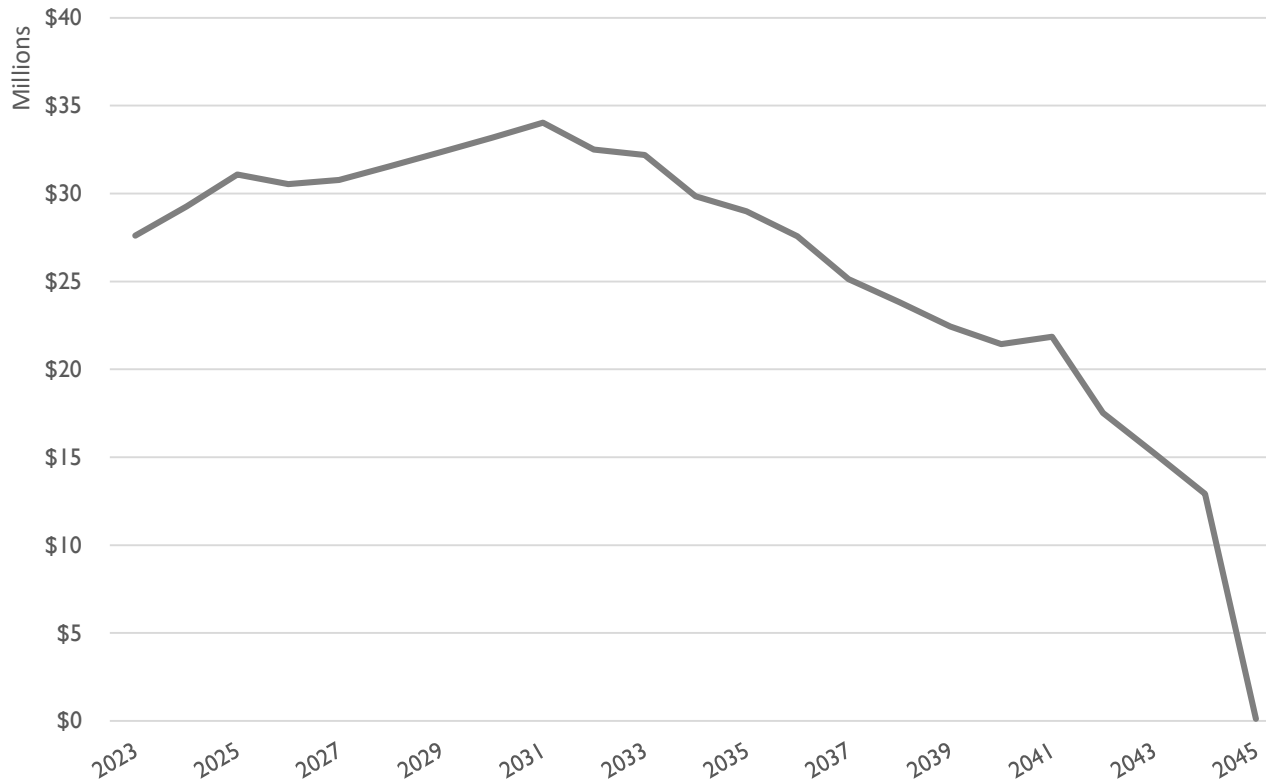
IMPACT FROM VARYING INVESTMENT RETURNS



CURRENT PAYMENT PLAN

CITY IS SCHEDULED TO PAY \$592 MILLION OVER NEXT 23 YEARS

Scheduled UAL Payments

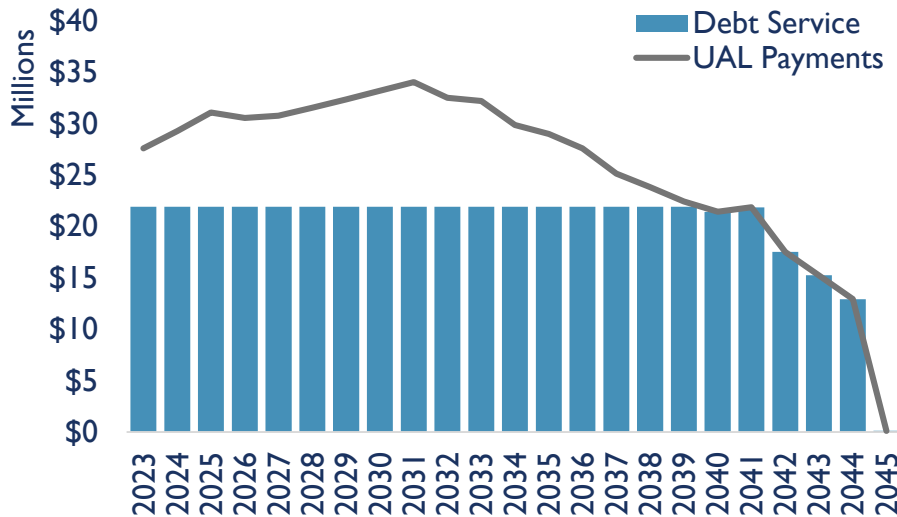


HYPOTHETICAL PENSION FINANCING

“MODIFIED LEVEL” STRUCTURING APPROACH

- Analysis assumes a refinancing of 100% of FY20 UAL
- Estimated to generate NPV savings of \$102.6 million

Estimated POB Payments at 100% UAL Funding



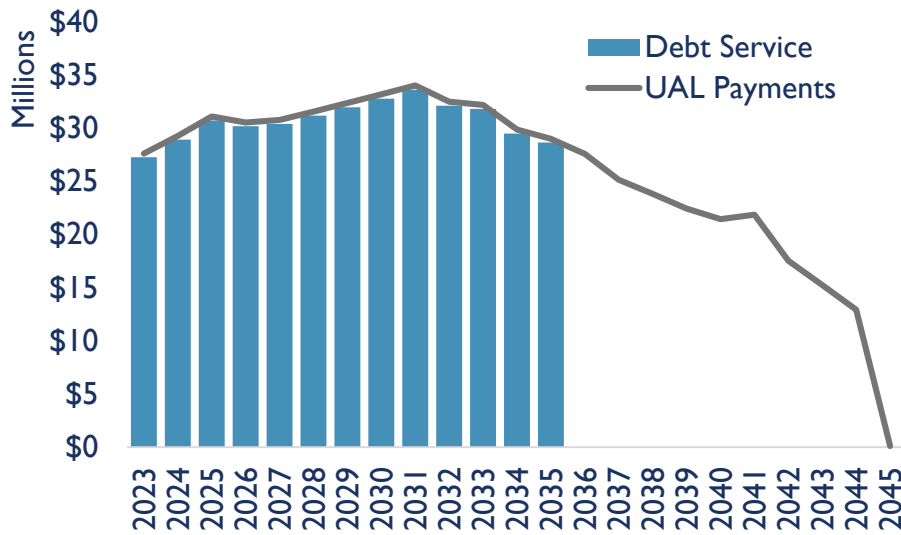
FY	UAL Payments	POB Payments	Gross "Savings"
2023	\$27,602,539	\$21,895,195	\$5,529,980
2024	29,260,907	21,897,923	6,912,464
2025	31,087,379	21,896,294	8,360,559
2026	30,538,546	21,897,214	7,616,207
2027	30,770,855	21,896,454	7,578,558
2028	31,551,298	21,896,422	7,988,840
2029	32,353,200	21,897,868	8,382,323
2030	33,177,153	21,897,776	8,761,958
2031	34,023,764	21,897,978	9,126,735
2032	32,492,578	21,893,770	7,729,512
2033	32,183,136	21,893,826	7,270,609
2034	29,849,030	21,893,872	5,446,567
2035	28,989,662	21,894,340	4,706,908
2036	27,574,698	21,898,341	3,648,571
2037	25,125,494	21,893,729	2,012,715
2038	23,824,987	21,897,200	1,163,298
2039	22,435,748	21,896,329	315,390
2040	21,427,846	21,423,820	2,281
2041	21,847,096	21,845,378	943
2042	17,519,760	17,519,593	89
2043	15,236,512	15,235,844	344
2044	12,916,455	12,915,155	649
2045	113,595	108,717	2,360
Totals	\$591,902,238	\$461,283,032	\$130,619,207
		NPV Savings (\$)	\$102,557,861
		NPV Savings (%)	31.14%
		All-In TIC	3.24%

HYPOTHETICAL PENSION FINANCING

“ACCELERATED” STRUCTURING APPROACH

- Analysis assumes a refinancing of 100% of FY20 UAL
- Estimated to generate NPV savings of \$121.7 million

Estimated POB Payments at 100% UAL Funding



FY	UAL Payments	POB Payments	Gross "Savings"
2023	\$27,602,539	\$27,268,476	\$334,063
2024	29,260,907	28,910,954	349,953
2025	31,087,379	30,714,085	373,294
2026	30,538,546	30,173,789	364,757
2027	30,770,855	30,398,245	372,610
2028	31,551,298	31,169,518	381,780
2029	32,353,200	31,965,177	388,023
2030	33,177,153	32,775,546	401,607
2031	34,023,764	33,611,980	411,784
2032	32,492,578	32,101,745	390,833
2033	32,183,136	31,797,201	385,935
2034	29,849,030	29,488,956	360,074
2035	28,989,662	28,641,164	348,499
2036	27,574,698	-	27,574,698
2037	25,125,494	-	25,125,494
2038	23,824,987	-	23,824,987
2039	22,435,748	-	22,435,748
2040	21,427,846	-	21,427,846
2041	21,847,096	-	21,847,096
2042	17,519,760	-	17,519,760
2043	15,236,512	-	15,236,512
2044	12,916,455	-	12,916,455
2045	113,595	-	113,595
Totals	\$591,902,238	\$399,016,836	\$192,885,403
		NPV Savings (\$)	\$121,699,646
		NPV Savings (%)	36.96%
		All-In TIC	2.83%

TIMELINE FOR ISSUANCE

PENSION OBLIGATION BONDS REQUIRE JUDICIAL VALIDATION

Judicial validation is utilized to begin the POB process

- This would allow the Agency to confirm that the pension liability is an obligation imposed by law and the POBs would be exempt from the Constitutional debt limit

The process for authorizing the POB would first require a resolution of issuance from the City Council followed by a 12-15 week review by Orange County Superior Court

Some cities are avoiding the validation process by issuing taxable lease revenue bonds

- This approach requires the use of leased assets

Timeline	Milestone
Week 1	<p>City Council approves financing and authorizes filing of validation action</p> <p>Complaint for validation filed</p> <p>Application to obtain order directing issuance, publication, and service of summons filed</p>
Week 2	<p>Hearing on application to obtain order directing issuance, publication, and service of summons held</p> <p>Special summons issued by Clerk of the Court</p>
Week 3	<p>Special summons published in newspaper for first time</p>
Week 6	<p>Request for entry of default against all persons filed</p>
Week 7	<p>Default entered against all persons by Clerk of the Court</p> <p>Default judgement package filed</p>
Week 8	<p>Hearing to request entry of default judgment of validation</p> <p>Default judgment of validation entered</p> <p>30-day appeal period begins</p>
Week 12	<p>Deadline to appeal default judgment of validation</p>

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