CITY OF CARSON

701 East Carson Street

Legislation Details (With Text)

File #:	2020-308	**Version:** 1	**Name:**		
Type:	Discussion		**Status:**	Agenda Ready	
File created:	5/12/2020		**In control:**	City Council	
On agenda:	5/19/2020		**Final action:**		

Title: APPROVAL OF RESOLUTION NO 20-082 RESOLUTION OF THE CITY COUNCIL OF THE CITY OF CARSON, CALIFORNIA, APPROVING THE FORM OF PRELIMINARY OFFICIAL STATEMENT IN CONNECTION WITH THE ISSUANCE OF THE CITY OF CARSON 2020 TAXABLE PENSION OBLIGATION BONDS AND APPROVING ADDITIONAL ACTIONS RELATED THERETO (CITY COUNCIL)

Sponsors:

Indexes:

Code sections:

Attachments: 1. Carson Pension Bonds Resolution no. 20-082 for OFFICIAL STATEMENT, 2. Carson 2020 POB Preliminary Official Statement Draft of May 14 2020 (Agenda)

Date	Ver.	Action By	Action	Result
5/19/2020	1	City Council		

Report to Mayor and City Council

Tuesday, May 19, 2020

Discussion

SUBJECT:

APPROVAL OF RESOLUTION NO 20-082 RESOLUTION OF THE CITY COUNCIL OF THE CITY OF CARSON, CALIFORNIA, APPROVING THE FORM OF PRELIMINARY OFFICIAL STATEMENT IN CONNECTION WITH THE ISSUANCE OF THE CITY OF CARSON 2020 TAXABLE PENSION OBLIGATION BONDS AND APPROVING ADDITIONAL ACTIONS RELATED THERETO (CITY COUNCIL)

I. <u>SUMMARY</u>

In January 2020, the City Council authorized the issuance of Pension Obligation Bonds (Bonds) to pay the unfunded actuarial liability (UAL) in the City's pension plan with the California Public Employees Retirement System (PERS) for the Miscellaneous employees' plan. At the same time, the City Council authorized the filing of a judicial validation action with the Los Angeles County Superior Court relating to the Pension Obligation Bonds.

The validation action is complete and the Bonds can now be issued. Approval of the Official Statement to be used in connection with the marketing of the Bonds is the final authorization needed to issue the Bonds.

II. RECOMMENDATION

1. Approve the resolution approving the form of a Preliminary Official Statement and the form of a Continuing Disclosure Certificate in connection with the issuance of the Bonds.

1.

III. ALTERNATIVES

Take another action deemed appropriate by City Council.

IV. BACKGROUND

In January 2020, the City Council authorized the issuance of the Bonds to prepay the outstanding unfunded liability (UAL) for the PERS plan for its general employees. As of June 30, 2018, the most recent PERS valuation date, the plan was 64.8% funded, with a net liability of approximately $107 million expected as of June 30, 2020.

In January, the estimated budget relief expected from issuance of the Bonds was approximately $45 million over 24 years. This was the difference between what would be required to be paid to PERS compared to the debt service on the Bonds. Those savings were based on assumptions relating to the City's credit rating and bond market conditions. Due to the COVID-19 pandemic, its effect on the City's finances in the short-term and its effect on the municipal bond market, the budget savings estimates have changed. The savings are now expected to be between $35 million and $37 million, as described below under the "Fiscal Impact" caption.

Although we are anticipating an increase in the unfunded actuarial liability used by CalPERS to determine future amounts owed by cities, increases in the UAL caused by the Fiscal Year 2019-20 CalPERS rate of return will not be determined until July 2021 and therefore is not included in the current Bond financing. Any UAL for the 2019-20 rate of return will begin affecting the cities' UAL costs starting in Fiscal Year 2021-22. This will occur even if the City does not issue the Bonds prepay the existing UAL.

Although the Bonds were authorized in January, the Bonds could not be issued until the completion of the judicial validation process, the timing of which was totally at the discretion of the court. That process was complete on May 1, 2020 and the City is currently in the 30 day waiting period before the judgment is official. At this time, there is only one remaining action needed by the City Council to issue the Bonds in June, to approve the Preliminary Official Statement to be used to market the Bonds to investors.

The Preliminary Official Statement is the offering document that provides investors with information about the City's finances, the impact of COVID-19 on operations and other security information concerning the Bonds.

The draft Preliminary Official Statement has been prepared with input from staff, financial advisors and attorneys. It is presented at this meeting for the City Council to review.

V. FISCAL IMPACT

In January, the bond issue was expected to provide budgetary savings to the City of up to $45 million dollars compared to the PERS payment schedule. This savings was based on a bond size of $108.3 million to pay both the UAL and expected costs of issuance. Based on updated assumptions, the budget relief is anticipated to be between $35 million and $37 million.

In January, the debt service on the Bonds was structured to be level at an estimated $7 million in every year through 2040 and declining thereafter, consistent with the decline in those 6 remaining years to match the PERS payment schedule. The level payment structure provided future budgetary certainty and avoided the annual increase in payments under the PERS system. This structure reduced the pension payment by about $800,000 in 2021, with increasing budget savings every year until they peaked in 2033 at $4.1 million compared to the PERS payment schedule.

As presented at to City Council in January, the estimated reduction PERS UAL costs were based on a 3.61% effective interest rate, and were approximately 22% compared to the PERS required payments.

Since that time, COVID-19 has impacted the City's finances as well as the bond market. The bond market is still fragile, and market sentiment and investor interest changes day to day. There were no Pension Obligation Bonds sold since the market crash in mid-March until April 22 (the day following the last interim update to the City Council). The rate on those bonds was considerably higher than expected on April 21. Therefore, to be conservative, the projected savings have been updated to use a 3.98% effective rate based on a AA- rating, compared to 3.61% used in the January estimates. This change in interest rate reduces the budget savings by approximately $4.8 million to $39.8 million, based on the same level debt service structure, with annual payments of $7.25 million instead of $7 million. The overall payment savings in this analysis is 19.5%.

Since COVID-19 has such a significant impact on the City's finances, staff looked at different structures that deferred some principal payments on the Bonds in the early years to provide reduced debt service in the first several years, slowly increasing until level debt service payments were again achieved after 5 years. The structure that staff is recommending provides a balance between the important objective of closing the City's budget gap for 2020-21 by reducing debt service and maintaining the integrity of the original structure to provide pension cost stability using a level, predictable annual payment.

The structure that is recommended is to pay no principal in 2020-21, a small principal payment in 2021-22, with principal increasing by $1.5 million each year in the next 3 years until debt service levels off in 2024-25 at $8.1 million. This equates to an additional $4 million reduction in payments in 2020-21 and a total reduction in the first 4 year of $7.4 million. This principal deferral will increase total debt service by $2.8 million because of the additional interest costs. The total savings would be $37 million in this scenario, based on a AA- rated bond. The structure reduces overall payment savings to 18.2%.

Although staff is recommending the structure described above, the structure can be modified if desired to extend the level payments to the last 6 years instead of reducing the debt service in later years to match the current PERS amortization. Bond Counsel is reviewing the authority to include capitalized interest in the financing to offset the first 18 months interest payments (resulting in no payment in 2020-21 and a lower payment in 2021-22), but has not reached a conclusion at this time. Both of these changes result in less overall savings, but impact specific years with additional savings early on or additional costs in later years. The City has another week to make the final structuring decision.

It is not certain that after the review by S&P of the City's finances and plan to deal with the COVID-19 impacts on the City's reserves in 2019-20 and 2020-21, as well as the potential unknown timing of a recovery of the local, regional and state economies, that the rating of AA- that the City anticipated rating will be achieved. The rating agency may in fact issue a lower rating, possibly A+. If the City's rating is A+, and the deferred principal structure described above is used, debt service on the Bonds would be based on an effective rate of 4.12%, and the savings would be reduced to $34.9 million. The City would still get the benefit of the reduced debt service of $7.4 million in the first 4 years. The overall payment savings in this analysis is 17.1%.

The table below shows the analysis for the AA- rated Bond, structured with no and low principal payments in the early years.

May 2020 Estimates; AA- Rating

FYE June 30	***UAL Payments***	***Debt Service***	***Reduction***
2021	7,800,842	3,721,000	4,079,842
2022	8,618,581	4,563,000	4,055,581
2023	9,284,153	6,051,000	3,233,153
2024	9,670,083	7,404,000	2,266,083
2025	10,114,816	8,084,000	2,030,816
2026	9,890,656	8,083,000	1,807,656
2027	9,977,460	8,080,000	1,897,460
2028	10,251,840	8,084,000	2,167,840
2029	10,533,767	8,081,000	2,452,767
2030	10,823,443	8,081,000	2,742,443
2031	11,121,087	8,081,000	3,040,087
2032	10,421,927	8,080,000	2,341,927
2033	10,261,326	8,083,000	2,178,326
2034	9,413,414	8,084,000	1,329,414
2035	9,062,837	8,085,000	977,837
2036	8,532,679	8,080,000	452,679
2037	7,630,590	7,630,000	590
2038	7,184,607	7,184,000	607
2039	6,708,324	6,705,000	3,324
2040	6,357,664	6,357,000	664
2041	6,158,081	6,154,000	4,081
2042	5,145,902	5,145,000	902
2043	5,225,106	5,224,000	1,106
2044	3,919,622	3,916,000	3,622

204,108,807	**167,040,000**	**37,068,807**

For every 1/4% increase or decrease in interest rates before the Bonds are sold, the reduction in payments will change by $3.8 million over the 24-year maturity of the POBs.

In summary, the changes to the budgetary relief estimates compared to the PERS existing payment schedule are as follows:

January estimated savings (AA- Rating)	$44,600,000
Reduction for Interest Rate Increase Since March	(4,800,000)
Reduction for Reduced Payments in Early Years	(2,800,000)
Revised Estimated Savings (AA- Rating)	$37,000,000
Potential Reduction for Interest Rate Increase (A+ Rating)	(2,100,000)
Revised Estimated Savings (A+ Rating)	$34,900,000

Future UAL

As of March 31, 2020, CalPERS estimated that the rate of return for its investment portfolio for the fiscal year-to-date was a negative 4%. There is no guarantee that CalPERS will achieve a better rate of return for the full fiscal year and it may be worse. Investment returns below 7% create additional liabilities for public agencies, including the City.

Any increase in the unfunded actuarial liability created by the Fiscal Year 2019-20 CalPERS rate of return will be determined in July 2021 and is not included in the current Bond financing. Any UAL for the 2019-20 rate of return will begin affecting the City's UAL costs starting in Fiscal Year 2021-22. This will occur even if the City does not issue the Bonds prepay the existing UAL.

VI. EXHIBITS

1. Resolution No. 20-082
2. Draft Preliminary Official Statement

Prepared by: Tarik Rahmani