



Legislation Text

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Report to Mayor and City Council

Tuesday, January 14, 2020

Discussion

SUBJECT:

APPROVAL OF RESOLUTION NO 20-015 OF THE CITY COUNCIL OF THE CITY OF CARSON, CALIFORNIA, AUTHORIZING THE ISSUANCE OF BONDS TO REFUND CERTAIN PENSION OBLIGATIONS OF THE CITY OF CARSON, APPROVING THE FORM AND AUTHORIZING THE EXECUTION OF A TRUST AGREEMENT AND BOND PURCHASE AGREEMENT, AUTHORIZING JUDICIAL VALIDATION PROCEEDINGS RELATING TO THE ISSUANCE OF SUCH BONDS AND APPROVING ADDITIONAL ACTIONS RELATED THERETO (CITY COUNCIL)

I. SUMMARY

At the November 26, 2019 City Council workshop, the City Council directed staff to prepare documents required to begin the process to issue Pension Obligation 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, with an estimated cost savings up to \$45 million over 24 years.

II. RECOMMENDATION

1. Approve the resolution (1) approving the form of a Trust Agreement and a Bond Purchase Agreement, (b) authorizing the issuance of the bonds in an amount not to exceed \$115 million, (c) authorizing the filing of a judicial validation action with the Los Angeles County Superior Court and (d) approving execution of related consulting contracts.

III. ALTERNATIVES

Take another action deemed appropriate by City Council

IV. BACKGROUND

At the November 5, 2019 Council Meeting, the City Council created an Ad Hoc Committee

to review cost effective pension liability funding opportunities. A presentation regarding pension liability funding was made at the November 19, 2019 City Council meeting. At that time, the City Council gave direction to conduct a public workshop on Pension Obligation Bonds (POBs). At the workshop, information was presented regarding POB issuance and potential financial benefits to the City from the issuance of POB. Based on the analysis, the cost to fund the existing UAL is estimated to be reduced by up to \$45 million over 24 years, with approximately \$31 million of that budget savings realized in the first 11 years.

The City has a PERS plan for its general employees, the “Miscellaneous Plan,” that includes all full-time employees and some part-time staff. 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.

The PERS required payment schedule to fund the liability creates a significant payment obligation in the next 10 years before payments start to decline. POBs are a debt management tool that will enable the financial impact of funding the \$107 million to be minimized over the next 11 years.

If the City were to issue POBs, based on current market conditions and estimated interest rates, debt service on the new POB would be approximately \$6.9 million declining in 2038 to match the existing UAL payments in later years, as shown in the table below under the “Fiscal Impact” caption.

The first step needed in the POB issuance process is to approve a form of a Trust Agreement and a Bond Purchase Agreement to submit for judicial validation by the court. The only issue that the courts will consider is the legal ability of the City to issue pension obligation bonds, and whether the sale meets the State of California constitutional and legal requirements. Any potential financial impacts are not part of the court’s analysis.

At the conclusion of the validation process, it is expected that the court will enter a judgment in favor of the City that the obligation of the City (the liability owed to PERS), legally represents an “obligation imposed by law”. Numerous prior court cases have determined that pension liabilities are obligations imposed by law, and therefore are exempt from the debt limitation requirements set forth in Article XVI, Section 18, of the California Constitution. Other cities have followed this same process for the issuance of pension obligation bonds.

The resolution presented authorizes the City Manager and the City Attorney to submit the necessary documents to the Los Angeles County Superior Court to start the judicial validation process as well as approves (1) the issuance of bonds in an amount not-to-exceed \$115 million, (2) a draft form of the Trust Agreement for the bonds (Exhibit 1) and (3) a draft form of the Bond Purchase Agreement for the bonds (Exhibit 2). The Trust Agreement identifies the duties and responsibilities of the trustee, establishes the terms and conditions under which the bonds are to be issued, and provides the security for the payment of the principal of and interest on the POBs. The Bond Purchase Agreement identifies the terms and conditions of sale of the POBs by the City to the Underwriters.

If the City Council approves staff’s recommendations, two concurrent processes will begin.

The first is the validation process referred to above, which takes a least 60 days and sometimes as much as 120 days (depending on the court's calendar). At the same time, staff and consultants will prepare other required financing documents and submit the financing to Standard & Poor's for a credit rating. It is important that these two processes run concurrently to expedite the final bond approval. To secure the lowest interest rate for the pension obligation bonds, staff is eliminating as much "down time" as possible in this issuance process.

The final actions to be taken by the City Council are expected be presented to the City Council in May 2020. The final actions to be taken include approval of the Preliminary Official Statement and specifying a not-to-exceed interest rate for the POB. The estimated savings from issuing the POB will be updated at that time based on changes in market conditions, and an expected actual bond size of \$108.3 million.

City Council directed staff to use the same financing team that recently completed the City's Measure M and Measure R financing, and to add Kosmont Transactions Services to the financing team. The City Council authorized the City Manager and City Attorney to enter into contracts with the participants and the resolution appoints Harrell & Company Advisors and Kosmont Transactions Services to provide financial advisory services, Aleshire & Wynder to provide bond counsel services, Nixon Peabody to provide disclosure counsel services and Cabrera Capital and Piper Sandler (formerly Piper Jaffray) to serve as Underwriters. These professional service agreements are on file with the City Clerk's Office.

V. FISCAL IMPACT

The bond issue will provide savings to the City of up to \$45 million dollars compared to the PERS payment schedule. This savings is based on a bond size of \$108.3 million to pay both the UAL and expected costs of issuance. This amount may change based on the discount rate (e.g., the implicit interest rate) used by PERS to value retirement benefits and the investment rate that PERS achieves in future years.

As presented at the City Council workshop, the current estimated reduction PERS UAL costs, resulting in budget relief to the General Fund, are shown below. Based on today's interest rates and an anticipated AA- credit rating, the budget savings are approximately 22% compared to the PERS required payments.

FYE June 30	UAL Payments	Debt Service	Reduction
2021	7,800,842	6,960,000	840,842
2022	8,618,581	6,963,000	1,655,581
2023	9,284,153	6,959,000	2,325,153
2024	9,670,083	6,960,000	2,710,083
2025	10,114,816	6,959,000	3,155,816
2026	9,890,656	6,963,000	2,927,656
2027	9,977,460	6,959,000	3,018,460
2028	10,251,840	6,961,000	3,290,840
2029	10,533,767	6,962,000	3,571,767
2030	10,823,443	6,961,000	3,862,443

2031	11,121,087	6,962,000	4,159,087
2032	10,421,927	6,959,000	3,462,927
2033	10,261,326	6,961,000	3,300,326
2034	9,413,414	6,960,000	2,453,414
2035	9,062,837	6,959,000	2,103,837
2036	8,532,679	6,963,000	1,569,679
2037	7,630,590	6,962,000	668,590
2038	7,184,607	6,959,000	225,607
2039	6,708,324	6,703,000	5,324
2040	6,357,664	6,355,000	2,664
2041	6,158,081	6,156,000	2,081
2042	5,145,902	5,142,000	3,902
2043	5,225,106	5,223,000	2,106
2044	3,919,622	3,915,000	4,622
	204,108,807	158,786,000	45,322,807

The effective interest rate for the POBs today is 3.61% including all costs of issuance. Interest rates can change between now and the anticipated bond issuance in June. For every ¼% increase or decrease in interest rates, the reduction in payments will change by \$3.8 million over the 24-year maturity of the POBs. Any PERS investment returns that are lower than the current 7% PERS assumption will add new UAL liabilities to be amortized over 20 subsequent years.

Other than the fees of the City's bond counsel, the consulting costs to issue the POBs (financial advisors, underwriter and disclosure counsel) are contingent on a successful bond issuance and payable from bond proceeds. The bond counsel fee is also payable from bond proceeds at closing.

The estimated fees also include rating agency fees, trustee fees and other costs of issuing the POBs. The underwriting costs are expected to be \$730,000 and the fixed costs are estimated to be \$450,000.

VI. EXHIBITS

1. Resolution no. 20-015 POB
2. City of Carson Bond Purchase Agreement
3. City of Carson Pension Bonds Trust Agreement
4. City of Carson Kosmont Financial Advisor Agreement Pension Bonds
5. City of Carson Nixon Peabody Disclosure Counsel Contract Pension Bonds

6. City of Carson Professional Services Contract Harrell Company

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