



Administrative Report

N.1., File # 21-2663

Meeting Date: 6/15/2021

To: MAYOR AND CITY COUNCIL
From: MARNI RUHLAND, FINANCE DIRECTOR

TITLE

DISCUSSION AND POSSIBLE ACTION REGARDING THE ISSUANCE OF LEASE REVENUE BONDS SERIES 2021A (FEDERALLY TAXABLE) BY THE REDONDO BEACH COMMUNITY FINANCING AUTHORITY

ADOPT RESOLUTION NO. CC-2106-065, A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF REDONDO BEACH, CALIFORNIA, APPROVING THE ISSUANCE OF LEASE REVENUE BONDS SERIES 2021A (FEDERALLY TAXABLE) BY THE REDONDO BEACH COMMUNITY FINANCING AUTHORITY; AUTHORIZING AND APPROVING A SITE AND FACILITY LEASE, A LEASE AGREEMENT, A PRELIMINARY OFFICIAL STATEMENT, A FINAL OFFICIAL STATEMENT, A CONTINUING DISCLOSURE AGREEMENT, A BOND PURCHASE AGREEMENT; AND AUTHORIZING CERTAIN OTHER ACTIONS IN CONNECTION THEREWITH

EXECUTIVE SUMMARY

In February 2021, the City Council directed staff to work with the City's Bond Financing Team to structure a bond financing to refinance the City's Unfunded Accrued Liability ("UAL") with the California Public Employees' Retirement System ("CalPERS"). As reported to the Council, the City is expected to achieve substantial budgetary savings by refinancing its pension obligation. This item presents the Lease Revenue Bond financing documents needed for City Council to officially authorize the refinancing.

BACKGROUND

The City's pension plan is managed under contract by CalPERS. The City's annual pension payments to CalPERS consist of two components which include the Normal Cost and the UAL. The normal cost is the amount CalPERS charges the City, as a percentage of its payroll, that is estimated to annually fund a share of all future pension obligations. The UAL repayment portion is the amount that is charged to the City to repay the City's estimated long-term UAL that is owed to CalPERS for past changes in benefits, underperforming CalPERS investment returns, and changes in the discount rate.

The UAL represents the difference between the amount necessary to pay actuarially determined future benefits already earned by current and former employees and the market value of the assets currently on deposit with CalPERS. The City's UAL constitutes a debt that must be repaid to CalPERS, and it is listed as a liability on the City's balance sheet in accordance with the

Governmental Accounting Standards Board (GASB) requirements. CalPERS currently charges the City 7% interest on this debt and has a repayment structure that will result in a large increase in annual pension costs over the next 10 years. As in many other cities in California, the growing obligations related to employee retirements represent a significant financial burden to the City. According to the most recently available CalPERS actuarial report (representing CalPERS performance and benefit cost estimates through FY 2018-19), the City's annual UAL repayment will increase from approximately \$13.7 million in FY 2020-21 to a high of \$21.5 million in FY 2030-31, an increase of 57%.

CalPERS calculates the actuarial value of benefits owed to plan members and the market value of plan assets annually, but it takes them one year to publish results. In other words, actuarial value of benefits owed to members and the market value of assets available as of June 30, 2019 were reported to the City in July of 2020, and they projected the UAL for June 30, 2021. The projected UAL balance at June 30, 2021 is the amount used to create the amortization schedule for Fiscal Year 2021-22 and beyond.

This means that the CalPERS results for the fiscal year ended June 30, 2020 will be reported to the City in approximately August of this year. Since CalPERS' investment returns for that year did not meet its 7% target, there will be another UAL base created. It is estimated that this new UAL will be somewhere in the range of \$10-\$15 million for the investment portfolio alone. Demographic and other changes that are currently being calculated by CalPERS could further increase this amount.

Current taxable municipal bond rates are substantially lower than the 7% CalPERS is charging the City. By issuing its own obligations to finance the UAL (instead of continuing to make installment payments to CalPERS on its terms), the City can realize substantial budgetary savings and better manage future pension costs. Obligations that are issued to finance a UAL must be issued at taxable interest rates.

In February 2021, the City Council directed staff to assemble a financing team to evaluate a potential issuance of bonds to refinance the City's UAL with CalPERS. At last week's Council Meeting, the financing team presented alternative approaches to refinancing the UAL which included the choice of Pension Obligation Bonds (POB) or Lease Revenue Bonds (LRB), different repayment structures and different plan funding options. At this meeting, the City Council directed staff to structure an LRB financing that would bring plan funding levels to 100% and to structure repayments in a fashion that would be level up-front and decline in a manner that was similar to that of the current CalPERS UAL amortization payment schedule.

Summary of Financing

The proposed financing is in the form of LRBs to be issued by the Redondo Beach Community Financing Authority (CFA). The City and CFA will enter into a Site and Facilities Lease to transfer certain leased properties of the City to the CFA, and the City will lease the same properties back from the CFA via a Lease Agreement. The City will agree to make semi-annual lease payments to the CFA, and the CFA in turn will use said lease payments to be received from the City as collateral to issue its LRBs in the capital markets.

The property to be leased under the leases will consist of various City streets that will be determined to have adequate value to satisfy legal and marketing requirements. Valuation of the leased properties will be performed by Kosmont Companies. The LRB proceeds will be used to repay CalPERS the total amount of the June 30, 2021 projected UAL, and possibly also the project UAL to be reported to the City in the near future, as may be directed by the City Council.

Structure Options

The City has several options in choosing the final structure. The Resolutions and estimate were prepared in a manner to allow the City maximum flexibility in its choices.

UAL

Bringing the City's plan funded status to 100% would also mean including the additional UAL that will be reported to the City near the end of this summer. With the issuance of LRBs, the City has the option to fund the anticipated UAL amount and forward the monies to CalPERS as soon as CalPERS reports the additional amount. If there are additional bond proceeds, the City will be able to apply them to bond payments. The actual sizing of the financing will be determined as the sale date approaches, which is currently scheduled for July 13.

The primary options the City has to consider are as follows:

Sizing

- Refinance all of the June 30, 2021 UAL only.
- Refinance all of the June 30, 2021 UAL plus the estimated June 30, 2022 UAL (Recommended).

FY 2021-22 Payments

- Schedule payments such that FY 2021-22 payments are approximately the same as the next subsequent years' payments (which are estimated to be \$13M to \$13.8M per year).
- Schedule payments such that FY 2021-22 payments are less than the next subsequent years' payments. (A \$12.5 million bond payment was recommended in the City Manager's proposed budget.)
- Schedule an interest only payment (of approximately \$5 million) for FY 2021-22. (Beyond what is identified in the proposed budget, this would allow the Council to use additional one-time General Fund savings of up to roughly \$6 million for other one-time Capital or Operating Budget items.)
- Fund interest payments with bond proceeds (i.e. capitalize interest payments) such that the City's budget will make no bond payments in FY 2021-22. (This would allow the Council to use additional one-time General Fund savings up to roughly \$10 million for other one-time Capital or Operating Budget items, but could negatively impact Standard and Poors' impression of our LRB Structure).

Repayments

- To keep payments lower, repay bonds on a "level" debt service basis

- To repay the LRBs more quickly, front-load the repayments and have payments in later years taper off (the so-called “hybrid or hybrid modified” structure) (Recommended)

Comprehensive repayment and structuring options will be presented to the City Council and CFA on June 15th.

COORDINATION

Transaction support has been provided by Kosmont Transaction Services as the City’s Financial Advisor. Additional transaction team members include Norton Rose Fulbright LLP (Bond Counsel); Richards Watson & Gershon (Disclosure Counsel); US Bank National Association (Trustee), and Stifel and Ramirez (Joint Underwriters).

FISCAL IMPACT

Savings from refinancing the CalPERS UAL will depend on the structure options chosen, and the impact to the FY 2021-22 budget will result in General Fund savings between \$2 million to \$10 million, also depending on the repayments and structure options ultimately chosen by the City Council.

APPROVED BY:

Joe Hoefgen, City Manager

ATTACHMENTS

Resolution Approving the Issuance of Lease Revenue Bonds
Site and Facility Lease
Lease Agreement
Preliminary Official Statement
Bond Purchase Agreement