Moore, Tania

From: Estanislau, Robin
Sent: Monday, March 1, 2021 2:06 PM
To: Moore, Tania
Subject: FW: Pension Obligation Bonds . . .

Robin Estanislau, CMC, City Clerk
City of Huntington Beach
714-536-5405

Please consider the HB City Clerk's office for your passport needs!

SUPPLEMENTAL COMMUNICATION

Meeting Date: 3/1/2021

Agenda Item No.: 19(21-177)

From: Fikes, Cathy <CFikes@surfcity-hb.org>
Sent: Monday, March 1, 2021 1:59 PM
To: Estanislau, Robin <Robin.Estanislau@surfcity-hb.org>
Subject: FW: Pension Obligation Bonds . . .

From: Gino J. Bruno <gbruno@socal.rr.com>
Sent: Friday, February 26, 2021 4:30 PM
To: CITY COUNCIL <city.council@surfcity-hb.org>
Cc: Chi, Oliver <oliver.chi@surfcity-hb.org>; Bulosan, Dahle <DBulosan@surfcity-hb.org>
Subject: Pension Obligation Bonds . . .

Mayor and Council members . . .

With respect to the proposed pension obligation bonds scheduled for your vote this Monday evening (March 1st), please demand a Study Session that is balanced with presentations of both the pros and – perhaps more importantly - the cons, such that you can take informed and knowledgeable votes.

As you should know, POBs have been described as a form of arbitrage, or trying to borrow money at low interest rates, invest the proceeds for higher returns, and use the differential to pay down the City's unfunded pension liabilities ($436 Million, as of June 2019), and ultimately repay the principal amount borrowed.

One organization (among many) to oppose the pension obligation bonds scheme is the *Government Finance Officers Association* (GFOA) that ***RECOMMENDS THAT STATE AND LOCAL GOVERNMENTS DO NOT ISSUE POBs***. The GFOA is a professional association of approximately 19,000 state, provincial, and local government finance officers in the United States and Canada headquartered in Chicago. It is the successor to the National Association of Comptrollers and Accounting Officers which was formed in February 1906. So they have some credibility, knowledge and expertise in these POB matters . . . and maybe our City Council should listen to them, as balanced against the presentations by bond underwriters and bond counsel who are not exactly disinterested presenters.

Here's a portion of how GFOA looks at these long-term pension obligation bonds, and why they are a bad risk:

Pension obligation bonds (POBs) are taxable bonds that some state and local governments have issued as part of an overall strategy to fund the unfunded portion of their pension liabilities by creating debt. The use of POBs rests on the assumption that the bond proceeds, when invested with pension assets in higher-yielding asset classes, will be able to achieve a rate of return that is greater than the interest rate owed over the term of the bonds. HOWEVER, POBS INVOLVE CONSIDERABLE INVESTMENT RISK, MAKING THIS GOAL VERY SPECULATIVE. Failing to achieve the targeted rate of return burdens the issuer with both the debt service requirements of the taxable bonds and the unfunded pension liabilities that remain unmet because the investment portfolio did not perform as anticipated. In recent years, local jurisdictions across the country have faced increased financial stress as a result of their reliance on POBs, demonstrating the significant risks associated with these instruments for both small and large governments.

The Government Finance Officers Association (GFOA) recommends that state and local governments do not issue POBs for the following reasons:

1. The invested POB proceeds might fail to earn more than the interest rate owed over the term of the bonds, leading to increased overall liabilities for the government.
2. POBs are complex instruments that carry considerable risk. POB structures may incorporate the use of guaranteed investment contracts, swaps, or derivatives, which must be intensively scrutinized as these embedded products can introduce counterparty risk, credit risk and interest rate risk.
3. Issuing taxable debt to fund the pension liability increases the jurisdiction's bonded debt burden and potentially uses up debt capacity that could be used for other purposes. In addition, taxable debt is typically issued without call options or with "make-whole" calls, which can make it more difficult and costly to refund or restructure than traditional tax-exempt debt.
4. POBs are frequently structured in a manner that defers the principal payments or extends repayment over a period longer than the actuarial amortization period, thereby increasing the sponsor's overall costs.
5. Rating agencies may not view the proposed issuance of POBs as credit positive, particularly if the issuance is not part of a more comprehensive plan to address pension funding shortfalls.

See: https://www.gfoa.org/materials/pension-obligation-bonds

In a commentary published December 31, 2019 in the *OC Register*, our former City Treasurer and now OC Treasurer/Tax Collector Shari Freidenrich was quoted as saying, "Surf City is risking a fiscal wipeout if it approves a proposal for pension obligation bonds." She goes on to say, "This scenario is reminiscent of the 1994 Orange County bankruptcy."

For her reasoning, as well as that of former Senator John Moorlach, see, https://www.latimes.com/socal/daily-pilot/opinion/story/2019-12-31/commentary-huntington-beachs-pension-bond-proposal-feels-like-deja-vu

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On June 14, 2020 the *Howard Jarvis Taxpayers Association* published a piece in which it explained, among other things:

"Advocates of this [POB] strategy rely on an assumption that the borrowed money from the sale of bonds, when invested with pension assets in higher-yielding assets, will achieve a rate of return that is greater than the interest rate owed on the borrowed money, which is paid back over the term of the bonds." Citing the *Government Finance Officers Association*, the HJTA went on to say, "The invested POB proceeds might fail to earn more than the interest rate owed over the term of the bonds, leading to increased overall liabilities for the government," and "issuing taxable debt to fund the pension liability increases the jurisdiction's bonded debt burden and potentially uses up debt capacity that could be used for other purposes. In other words, the government could lose money on the deal, become overextended on its credit which would, in turn, 'crowd out' the ability to fund essential services."

Amongst other position papers the HJTA has published in reasoned opposition to POBs, see https://www.hjta.org/california-commentary/states-ongoing-fight-over-pension-obligation-bonds/

Again, please delay this important vote involving $436 Million of taxpayer moneys, demand a balanced Study Session, conduct your own independent research, and vote wisely.

Thank you.

Gino J. Bruno
Huntington Beach