

1. Why is funding retirement pensions an issue?

The State of California has \$160 billion total unfunded pension liability, and most California cities are facing this issue.

Since 2018, the Oxnard City Council has been hosting public study sessions relating to the rising pension costs. Potential cost management strategies, including the concept of restructuring the Unfunded Accrued Liability (UAL), were most recently discussed by the Council Finance and Governance Committee on Feb. 8, 2022, and later by the full City Council on March 1, 2022. In a 7-0 vote, the Council voted to initiate the Pension Obligation Bond (POB) validation process.

2. What is unfunded pension liability?

The official term for this is called Unfunded Accrued Liability (UAL), which is the shortfall between money the City has invested with the California Public Employees' Retirement System (CalPERS) and the amount required to fully pay out the benefits that are legally obligated to retirees.

3. How much is Oxnard's UAL?

\$322 million.

4. What is a Pension Obligation Bond (POB)?

A POB is a taxable bond that the City issues to investors. The proceeds that the City raises are then sent to CalPERS to extinguish all or a part of the City's current UAL. Often, a POB is referred to as a UAL Refinancing or UAL Restructuring.

5. Are other cities in California doing this?

Yes. Approximately 90 CalPERS members have recently issued bonds to restructure their UAL. Several cities that have pension tax overrides similar to Oxnard's have issued POBs.

6. Will invested pension bond proceeds potentially earn less than the borrowing costs?

Yes. Instead of CalPERS's expected earnings rate of (currently 6.8%), lower actual returns could occur. The chances of long-term returns being below current < 4.00-4.50% borrowing costs do exist.

A "stress testing" process is often helpful to better quantify this risk and understand the impacts of CalPERS underperformance under a multitude of scenarios, both with and without a POB. Each agency has different risk tolerances.

As discussed in the previous workshops, the City of Oxnard intends to conduct a robust stress testing process with their actuary to quantify these risks, potential outcomes, and then decide if a POB is recommended or not based on those results.

7. Do today's pension bonds carry the risk of swaps or derivatives?

No. Only fixed-rate POBs (this means no swaps or derivatives) are being issued in the current marketplace. Some POBs issued 15-20 years ago did involve swaps and derivatives.

8. Will issuing taxable debt to fund the pension liability increase the jurisdiction's bonded debt burden and use up the City's debt capacity?

No. POBs replace CalPERS (all or portion) UAL on the agency's balance sheet, thereby converting one liability into another.

9. Aren't pension bonds typically issued without call options? Won't this make it more difficult to refund bonds if interest rates fall or a different debt service structure is desired in the future?

No. All POBs are issued with an optional redemption (5 or 10 year call) in the current marketplace for flexibility to refinance or pay off early at no penalty.

Nearly all POBs issued prior to 2017 were not callable or required a penalty to pay off. Oxnard would only issue a POB if it had a flexible call option.

10. Are pension bonds structured in a manner that defers the principal payments?

No. Almost all POBs amortize principal immediately. Shortening, lengthening, or maintaining the same term of payments is at the discretion of each agency since each has different budgetary objectives and constraints.

11. Won't rating agencies view the proposed issuance of pension bonds as credit negative?

No. Rating agencies have noted the positive benefits of a POB that is prudently structured from a thoughtful and comprehensive policy to increase payment affordability, financial flexibility and long-term resiliency. A Pension Funding Policy is noted as a credit positive by S&P.

12. Is the Government Finance Officers Association (GFOA) against POBs?

The GFOA has advised municipalities not to issue POBs. In their reports from 2015 and [2021](#), they cite six reasons why they do not recommend POBs.

The City has reviewed each reason with its advisory team and found only one of those concerns is applicable: That there is risk that the pension fund may not earn more than the interest rate paid on the bond over the life of the bond.

This is the core risk of any POB, and it's being analyzed in depth by the City, its financing team and its third party actuarial expert. Interest rates, bond structuring strategies and risk mitigation techniques all play a critical part in this risk assessment.

The GFOA's stance is rather narrow and does not include discussion of any of these factors that impact risk. There are other financial organizations that, in the opinion of the City, have provided a more comprehensive assessment of POBs in the current market, such as the whitepaper developed by the [Illinois Public Pension Fund Association](#).

Additionally, the GFOA opinion does not differentiate between the types of pension bonds issued in different states, the structures of each, and the strategies utilized.

For example, one reason so many agencies have restructured their CalPERS UAL in California is due to the highly uneven and spiking repayment shape required by CalPERS. In addition to the potential interest rate benefit, the strategy of smoothing out these uneven and peaking payments to better enhance budget predictability, fiscal sustainability, and reduce the tax burden on residents are also key objectives the City is evaluating.

In order for the City to even consider a POB, it must initiate a POB validation process. Concurrently with this process, the City can evaluate the interest rates and bond market and *potentially* issue POBs if market conditions permit. The City will be continuously monitoring the economic viability (benefits/risks) of a POB during the validation process. Without the successful conclusion of the validation process, the City will not have the legal ability to issue a POB.