Opportunity Overview
Refinance CalPERS UAL with Pension Obligation Bonds

KPPCSD

KENSINGTON POLICE PROTECTION AND COMMUNITY SERVICES DISTRICT

MAY 14, 2020

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KOSMONT SERVICES OVERVIEW

KOSMONT COMPANIES
ADVISORY

Real Estate
Finance/Economics
Development
Entitlements

ECONOMIC DEVELOPMENT, REAL ESTATE, PROJECT FINANCE, AND IMPLEMENTATION STRATEGIES

- Public / Private Transactions
  Structuring / Negotiation / Entitlements
- Developer Selection RFQ/P & ENA/DDA
- Project Funding / Financing Strategies
- TIF, EIFDs, CRIAs, Housing
  Sustainability & Housing Districts
- Kosmont Retail NOW!®
  Trends / Analytics / Recruitment
- Retail Predictive Intelligence (A.I.)
- Economic Development Strategies / Plans
- Market & Feasibility Analysis
- Fiscal Impact / Economic Benefit Studies

KOSMONT REALTY
BROKERAGE

REAL PROPERTY SALES, LEASING, AND ASSET BASED SERVICES

- Brokerage (CA DRE # 02058445)
- Real Estate Market Analysis
- Developer / Buyer Selection
- RFQ/P & ENA/DDA
- Ground Leases
- Zoning & Implementation Strategies
- Property Valuation / Broker Opinion of Value (BOV)
- Asset Management Plans
- www.OppSites.com
  (online economic development marketplace)

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PUBLIC FINANCE

PUBLIC FINANCE ADVISORY AND TRANSACTIONS SERVICES

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- General Fund Financings
  G.O.s / COPs / Lease/Leaseback
- Tax Increment Financing (TIF)
  EIFD / CRIA / Housing Districts
- Public/Private Partnerships (P3)
- Pension Obligation Bonds
- Lease Revenue Bonds
  JPAs / Pooled
- Utility / Enterprise Lease Financings
- Assessment / Special Tax / CFD
- Private Placements

Full Service * Integrated * Experienced

FIRM OVERVIEW

Kosmont Transactions Services, Inc. ("KTS") is one of three integrated Kosmont firms dedicated to the pursuit of Economic Development opportunities for our clients

EXECUTIVE SUMMARY

- Kensington Police Protection and Community Services District ("District") is a member of the California Public Employees' Retirement System ("CalPERS")
  - Covers public safety (police) employees
  - Two plans: "Classic" and "PEPRA"
- The District's "Classic" plan is substantially underfunded
  - Current Market Value of Assets is insufficient to meet the plan's Accrued Liability to its participants
  - Difference is called Unfunded Accrued Liability or UAL (=$4,434,254 as projected at 6/30/20)
- UAL is a debt owed to CalPERS that is being repaid at 7% interest rate
- Opportunity to refinance UAL by issuing Pension Obligation Bonds ("POBs") at 3.85% interest
- This presentation describes the opportunity, the process, the participants and anticipated benefits of issuing POBs to refinance the UAL debt at a lower interest rate

FINANCE TEAM MEMBERS AND RESPONSIBILITIES

- **KTS – Independent Registered Municipal Advisor to the District (Fiduciary)**
  - Assures District's financial and policy interests are protected
  - Intermediary between Placement Agent/Purchaser and District
  - Manages financial transaction details on behalf of District
- **Nixon Peabody – District Bond Counsel (Fiduciary)**
  - Attorney to the District; assures District's legal interests are protected
  - Prepares all legal documentation; assures bonds are "valid and legally binding obligations"
- **Brandis Tallman - Placement Agent**
  - FINRA member; acting as independent agent
  - Sources lender; negotiates terms between lender and District

STATUS OF DISTRICT'S UAL WITH CALPERS

- District's CalPERS Classic Safety Plan has a substantial UAL[1]
  - $4,270,379 at 6/30/18
  - **$4,434,254 projected at 6/30/20**
- District's UAL with CalPERS is an existing debt
- Unfunded pension liabilities are now required by GASB to be listed as current liabilities on public agencies' balance sheets, not just referenced in the notes
- CalPERS requires members to make annual payments to amortize UAL debt
  - Repayment schedule changes yearly rendering future UAL payments unpredictable
- According to CalPERS, overall pension costs likely to continue increasing for 10 years due to unfunded liabilities[2]

[1] Source: CalPERS, *Actuarial Valuation as of June 30, 2018 for the Safety Plan of the Kensington Community Services District*
[2] Source: CalPERS, "CalPERS CEPPT Program" presentation to the District of February 25, 2020

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CURRENT MARKET VOLATILITY LIKELY TO ADD TO UAL

- Market returns of less than 7% increase UAL
- CalPERS returns currently flat for the year
  - Value at market close 5/6/2020 = $371.1 Billion ("B"); value at 6/30/2019 was $372.6 B[1]
  - Hit record high value of $404 B in February; down as much as $69 B in recent market downturn
- How does recent market volatility impact the District?
  - Savings from POB are calculated based on 6/30/20 projected UAL being amortized (i.e. $4,434,254)
  - Recent market losses don’t impact the POB estimated savings analysis for current UAL
  - With or without a POB, the District's UAL seems likely to increase based on current market activity

[1]Source: CalPERS

OPPORTUNITY TO LOWER PENSION COSTS
REFINANCE CalPERS UAL WITH POBs

- UAL debt is being amortized at a high rate of interest (i.e. CalPERS' Discount Rate, currently 7.0%)
- Issuing POBs to refinance all or a portion of District's UAL debt can significantly lower annual pension payments
- Municipal bond market interest rates are currently substantially lower than the CalPERS rate
- District has opportunity to lock in low refinancing rate right now
  - 3.85% rate of interest offered per Lender Term sheet submitted by Brandis Tallman (Placement Agent)
  - Utilize savings for current expenditures/projects, budget reserves, and/or to fund investment portfolio to further reduce future pension costs ("Section 115 Trust")

PRIVATE PLACEMENT POB
SUMMARY OF SAVINGS[1]

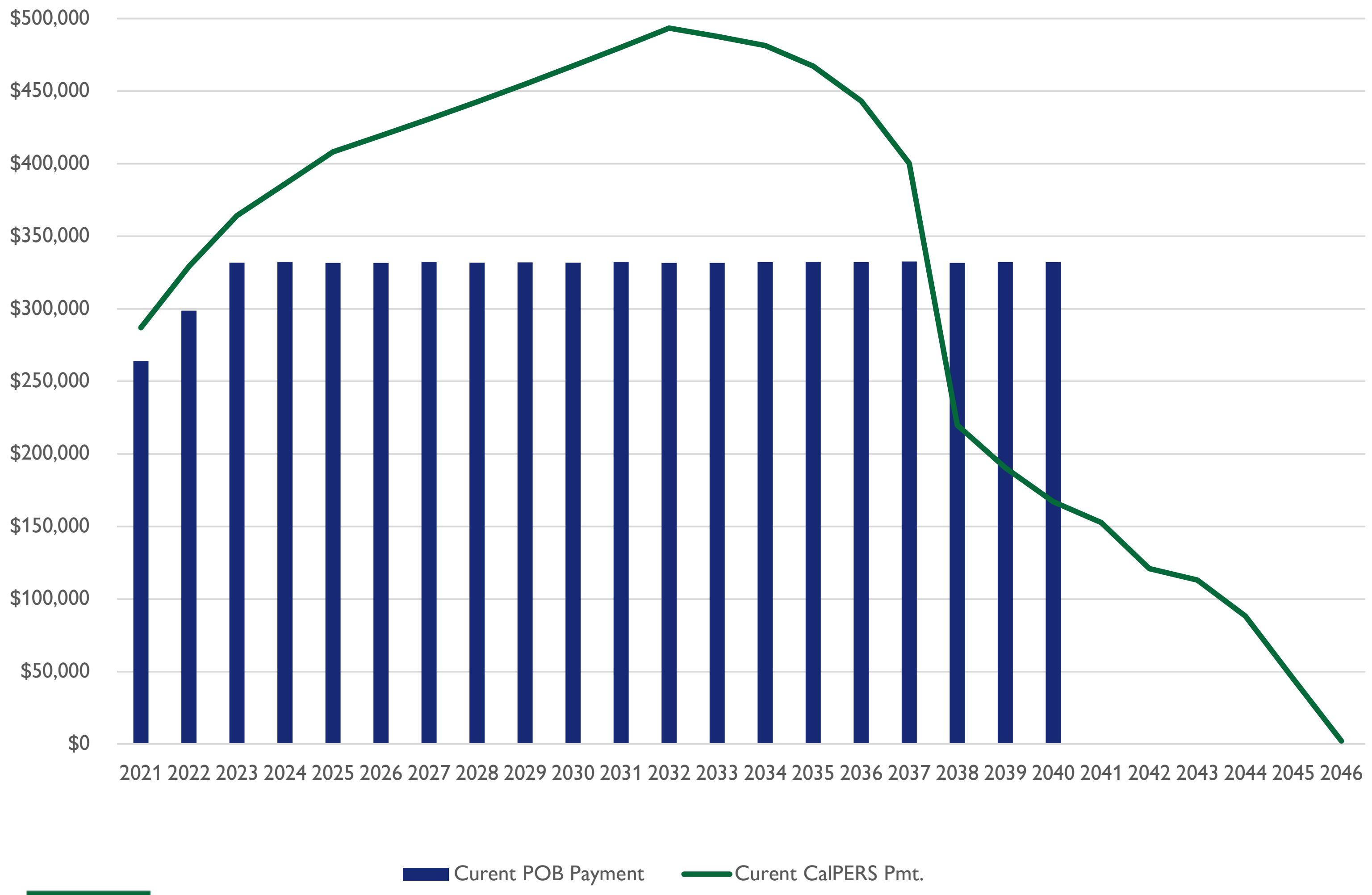
- 3.85% Interest Rate vs. 7.00% CalPERS amortization
- $1.8 million gross savings (budgetary) over remaining life
  - $22,000 in FY2021 increasing to max. of $162,000 in FY2032 annual (budgetary); varying thereafter with some years of "dis-savings" due to level POB payments vs. declining CalPERS payments in later years
- $1.172 Net Present Value savings yielding NPV% savings of **26.42**%
- Closing must occur by June 18, 2020

[1] Savings Compared to current CalPERS amortization as presented in *Actuarial Valuation as of June 30, 2018 for the Safety Plan of the Kensington Community Services District*; CalPERS amortization will change year to year; these comparisons represent a "snapshot" compared to current assumptions

PRIVATE PLACEMENT POB OPPORTUNITY
SUMMARY OF PRIMARY FINANCING TERMS

- General Obligation debt, but not "unlimited ad valorem tax" pledge
- 20-year repayment term
  - 6 years shorter than current CalPERS repayment assumptions
- POB to be repaid via "Level Debt Service" structure
  - Unlike current projections which call for dramatic increases, POB payments will be smoothed out
  - Principal paid annually; interest paid semiannually
- 10-year call option
  - Option to redeem or refinance in 10 years if District's financial condition or market conditions favor
- No Debt Service Reserve Fund or additional required security required beyond "obligation to pay"
- $120,000 approximate issuance costs
  - Paid through the financing; no out-of-pocket costs to the District whatsoever
- **Close by 6/18/20**

UAL/POB REPAYMENT COMPARISON



Year Ending 30-Jun	Curent CalPERS Pmt.	POB Payment	**Savings**	Net Present Value Savings
2021	$287,011	$264,016	**$22,995**	$22,115
2022	329,254	298,823	**30,431**	28,182
2023	364,295	331,818	**32,477**	28,962
2024	386,173	332,350	**53,823**	46,217
2025	408,112	331,612	**76,500**	63,254
2026	419,335	331,644	**87,691**	69,820
2027	430,866	332,406	**98,460**	75,488
2028	442,715	331,860	**110,855**	81,840
2029	454,890	332,044	**122,846**	87,330
2030	467,399	331,921	**135,478**	92,740
2031	480,253	332,489	**147,764**	97,400
2032	493,460	331,711	**161,749**	102,666
2033	487,781	331,625	**156,156**	95,441
2034	481,417	332,193	**149,224**	87,824
2035	467,368	332,375	**134,993**	76,503
2036	443,165	332,173	**110,992**	60,570
2037	400,229	332,585	**67,644**	35,545
2038	219,882	331,574	**(111,692)**	(56,516)
2039	190,383	332,178	**(141,795)**	(69,088)
2040	167,074	332,320	**(165,246)**	(77,530)
2041	152,666	0	**152,666**	68,972
2042	120,887	0	**120,887**	52,590
2043	113,079	0	**113,079**	47,370
2044	88,295	0	**88,295**	35,616
2045	44,964	0	**44,964**	17,465
2046	2,153	0	**2,153**	805
TOTALS	$8,343,106	$6,539,717	**$1,803,389**	$1,171,581

POTENTIAL POLICY CHOICES FOR USE OF SAVINGS

- ✓ Build up reserves
- ✓ Utilize savings for current expenditures or projects; budget increases; tax/fee reductions
- ✓ Fund investment portfolio to further reduce future pension costs
  - Typically called "Section 115 Trusts"; several products and options available
    - *PARS and CalPERS are popular program providers*
  - Financial products available to leverage savings for potential earnings potential
  - Potential for District to "self-manage" if desired
  - Discussion of Section 115 Trust options can be ongoing—beyond POB approach
- <u>District may wish to adopt a formal pension policy to memorialize the Board's choices</u>

POBs ARE INHERENTLY A DEFENSIVE FISCAL POLICY

- The District can refinance all or any portion of UAL
  - Determine policy for appropriate funding level of "Total Plan Liability"
- Savings can be used for any legal District purpose or to implement new fiscal policies
  - e.g., Potential to set up Section 115 Trust with additional cashflow
- Cost Savings with POBs can reduce impact of future CalPERS changes which typically increase pension costs, such as:
  - Mortality assumption changes requiring greater funding for longer retirement periods
  - Discount rate reductions requiring greater "Normal Cost" payments due to lower anticipated returns, increasing future contributions
  - Future newly created UALs (as anticipated this year) amortizing over shorter periods with no "ramp up", increasing amortization payments, further increasing Annual Required Contribution payments

SELECT LISTING OF POB ISSUES

RECENT PUBLIC OFFERINGS

City of Larkspur	$18,295,000	4/30/2020
County of Riverside	$719,995,000	4/22/2020
City of Pasadena	$131,805,000	2/5/2020
Monterey Cnty Reg. F.D.	$64,420,000	11/21/2019
City of Pacifica	$9,685,000	10/9/2019
City of Shasta Lake	$9,500,000	10/8/2019
City of Hawthorne	$121,865,000	9/24/2019
City of Marysville	$15,000,000	9/13/2019
City of Glendora	$64,420,000	8/22/2019
City of Chowchilla	$10,500,000	3/6/2019
City of Baldwin Park	$54,085,000	2/20/2019
City of La Verne	$54,265,000	7/26/2018
Tulare County	$251,220,00	5/31/2018

SPECIAL DISTRICT DIRECT PLACEMENTS BY BRANDIS TALLMAN

Richardson Bay Sanitation District

Central Fire Protection District

Stanislaus Fire Protection District

Pleasant Valley Recreation & Park District

Tehachapi Cummings County Water District

Truckee Donner Public Utility District

San Miguel Fire Protection District

Montecito Fire Protection District

Lakeside Fire Protection District

Monterey Peninsula Airport District

GFOA'S CONCERNS DON'T TRACK WITH CALIFORNIA POBs

- The Government Finance Officers Association ("GFOA") has a Best Practice/Advisory posted on its website that was adopted in January 2015 regarding the issuance of POBs that states "…GFOA recommends that state and local governments do not issue POBs…"
- The language chosen by GFOA to describe its position regarding POBs is limiting as it assumes all POBs are structured the same way, which is a fallacy, yet it blanketly admonishes against the use of anything called a "Pension Obligation Bond"
- Certain of GFOA's expressed concerns about potential pitfalls, however, are quite sound and was used as a guide to structure the Proposed POBs.
- **GFOA's primary reasons not to issue POBs and a description of how they are not applicable to California's version of POBs and the Proposed POBs are as follows:**

GFOA'S CONCERNS DON'T TRACK WITH CALIFORNIA POBs (cont.)

GFOA CONCERNS[1]	CALIFORNIA'S VERSION OF POBs
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	**Not Applicable; proceeds** will not be used to set up a separate investment fund; **only to repay CalPERS directly to refinance the existing UAL debt**
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.	**Not Applicable;** the Proposed POBs are 20-year, fixed-rate, fully amortizing bonds; proceeds will be used only to refinance existing UAL debt and pay issuance costs; **no derivatives, swaps or GICs will be used whatsoever**
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.	**Not Applicable;** (i) **UAL is existing debt; no new debt is being created** (ii) the Proposed **POBs have a call option whereby the District may redeem all the bonds then outstanding, at face value (i.e. a "par call"), after 10 years**, which mirrors standard practices in the tax-exempt bond market

[1] Source: "Pension Obligation Bonds", Government Finance Officers Association, January 2015, www.gfoa.org/pension-obligation-bonds

GFOA'S CONCERNS DON'T TRACK WITH CALIFORNIA POBs (cont.)

GFOA CONCERNS[1]	CALIFORNIA'S VERSION OF POBs
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	**Not Applicable;** the Proposed POBs: (i) repay the ULA using "level debt service" which smooths out the repayment, eliminating the extreme pension cost increases faced by the District over the next 10 years; and (ii) **the POBs will be fully repaid six (6) years sooner than the current UAL is projected to be repaid**
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	**Not Applicable** (also Obsolete); **Proposed POBs are** structured **as a direct (or "private") placement wherein one institution has offered to purchase the entire bond issue, eliminating the need to obtain a bond rating. The criteria of rating agencies has been revised since 2015** and issues structured like the proposed **POBs are now generally viewed as credit positive for the issuer**

[1] Source: "Pension Obligation Bonds", Government Finance Officers Association, January 2015, www.gfoa.org/pension-obligation-bonds

DISTRICT'S DECISION: POBs OR NOT?

RESULT/IMPACT OF REFINANCING UAL

- Reduces interest rate from 7% to 3.85%; >26% savings
- Future pension costs in short/medium term to repay existing UAL obligation will be dramatically reduced compared to current requirements
- Smooth out annual budgeted payment
- Private placement approach is a low-cost option available to select few agencies (Kensington qualifies)

RESULT/IMPACT OF STATUS QUO

- Continue to repay UAL at 7% interest rate
- Future pension costs in short/medium term to repay existing UAL obligation to dramatically increase according to current requirements
- Curve of repayment costs will be steep
- Opportunity for private placement and not guaranteed to remain available

NEXT STEPS

- ✓ Engage Finance Team
- Board presentation
- Draft legal documents
- Board considers authorization
- *Finalize transaction details (due diligence)*
- *Payoff UAL with CalPERS*

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PROJECTED SCHEDULE OF ACTIVITIES

WEEK OF	ACTIVITY
completed	Engage Finance Team
completed	Finance Committee presentation
May 11	Board of Directors presentation (May 14)
May 18	Prepare draft legal documents and authorizing resolutions
May 25	Board of Directors meet to consider authorization (May 28)
June 1	Due diligence; finalize all transaction documents
(Before June 18)	Close Pension Obligation Bonds; Pay off UAL to CalPERS

THANK YOU – ANY QUESTIONS?

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KOSMONT TRANSACTIONS SERVICES

MAY 14, 2020

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