City of Yuba City, California

Pension Liability Management Overview

AUGUST 9, 2022

CalMuni ADVISORS

Presenters

- Andrew Flynn, Managing Director

  California Municipal Advisors LLC – Independent Registered Municipal Advisor

  - Assures City's financial and policy interests are protected
  - Intermediary between Broker/Dealer or Placement Agent and City
  - Manages financial transaction details on behalf of City

Pension Funding Status

Description	Safety 1st*	Miscellaneous*	Safety 2nd*	PEPRA - Police	PEPRA - Fire	Police 3rd	Fire 3rd	Combined
Total Accrued Liability	$75,997,600	$138,161,258	$84,299,823	$1,622,820	$1,618,837	$2,090,873	$1,075,460	$304,866,671
Market Value of Assets	$47,829,617	$98,646,906	$64,280,286	$1,462,151	$1,478,493	$1,910,539	$987,179	$216,595,171
Unfunded Actuarial Liability (UAL)	**$28,167,983**	**$39,514,352**	**$20,019,537**	**$160,669**	**$140,344**	**$180,334**	**$88,281**	**$88,271,500**
% Funded	**62.9%**	**71.4%**	**76.3%**	**90.1%**	**91.3%**	**91.4%**	**91.8%**	**71.0%**

Source: CalPERS Actuarial Valuation as of June 30, 2020

** Included in analysis*

Definitions:

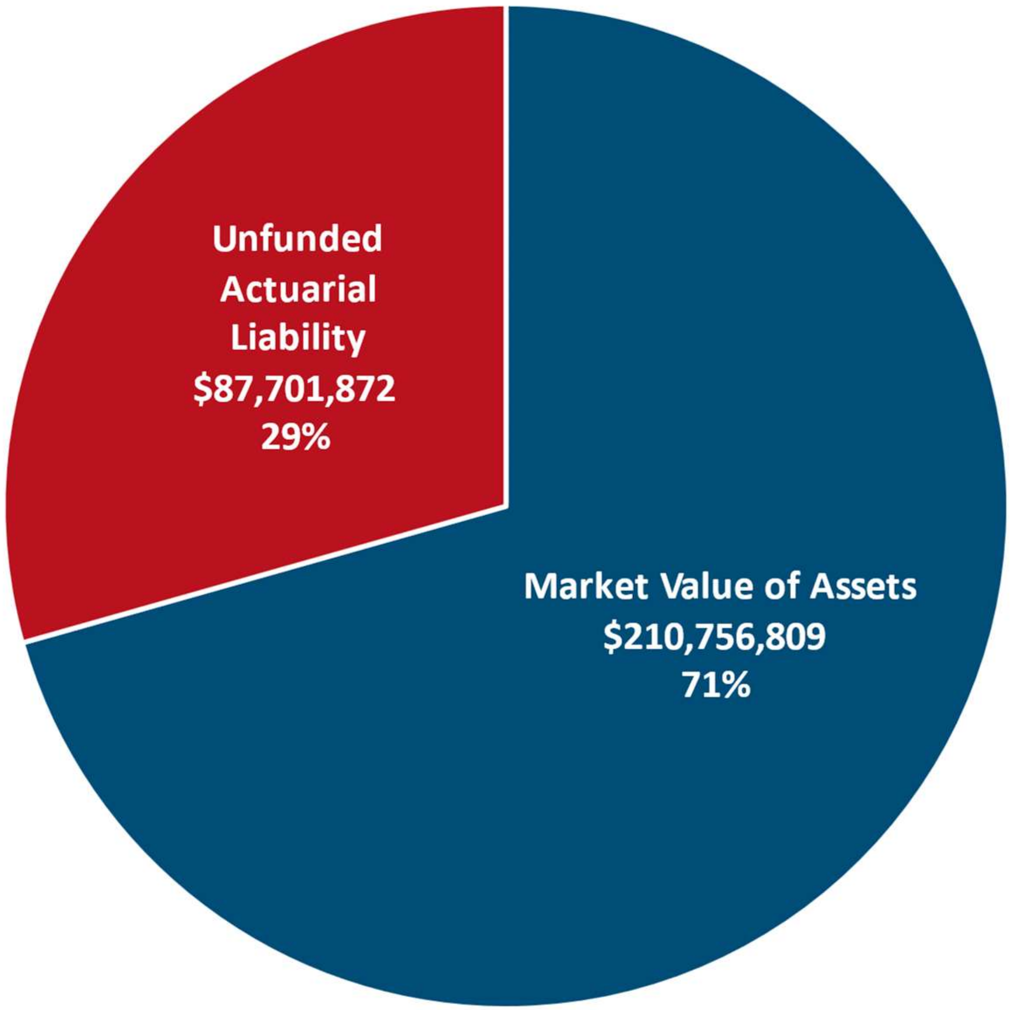
- Total Accrued Liability = What You Need
- Market Value of Assets = What You Have
- Unfunded Actuarial Liability = What You Owe

Seven Pension Plans:

- Classic: Safety 1st, 2nd, Miscellaneous, Police 3rd & Fire 3rd
- PEPRA: Police & Fire

Safety 1st, 2nd & Miscellaneous
represent a significant savings opportunity

Pension Funding Status

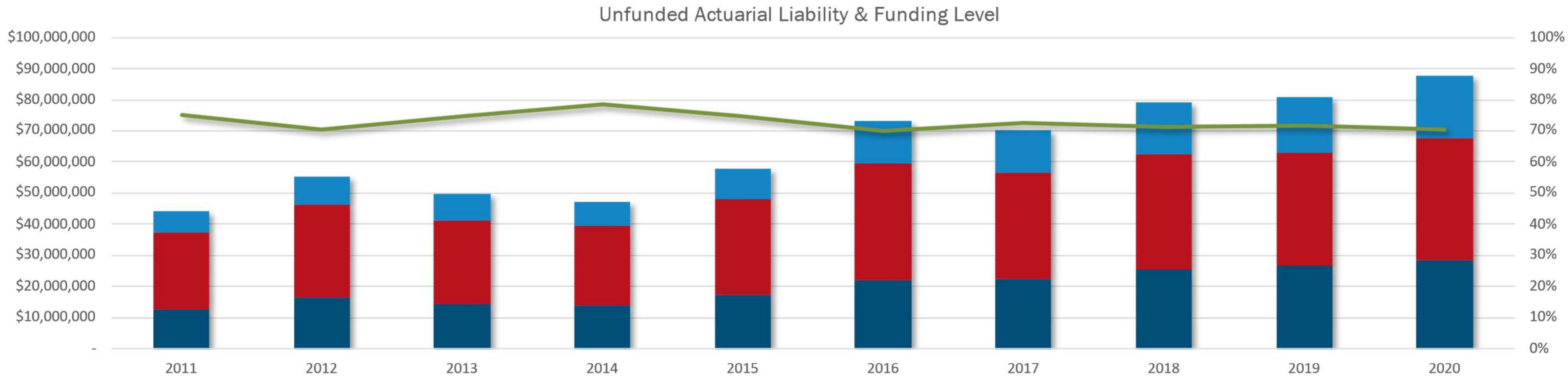


- Total Pension Obligations = $298.5M
- Pension Assets = $210.8M
- Shortfall = $87.7M (29.4% of what is needed)
  - Accrues interest at 7% interest rate = $68.3M interest
  - Total Unfunded Liability with interest = $156.0M

Shortfall (UAL) = DEBT:

- Amortizes over time (currently 25 years)
- Reduced or delayed payments not allowed
- City's most expensive debt
- No prepayment restrictions or penalties

Pension Funding History



	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Safety 2nd	$6,695,704	$9,192,392	$8,820,130	$7,722,208	$9,782,949	$13,755,897	$13,903,743	$16,659,216	$17,868,839	$20,019,537
Miscellaneous	$24,802,492	$29,836,882	$26,693,320	$25,789,074	$30,605,057	$37,385,807	$33,793,558	$36,851,053	$36,268,028	$39,514,352
Safety 1st	$12,550,758	$16,311,110	$14,364,212	$13,768,451	$17,478,511	$22,124,763	$22,606,593	$25,492,709	$26,542,609	$28,167,983
Total	**$44,048,954**	**$55,340,384**	**$49,877,662**	**$47,279,733**	**$57,866,517**	**$73,266,467**	**$70,303,894**	**$79,002,978**	**$80,679,476**	**$87,701,872**
% Funded	75.27%	70.61%	74.84%	78.44%	74.88%	70.01%	72.58%	71.36%	71.81%	70.62%

Owe

$43.6M

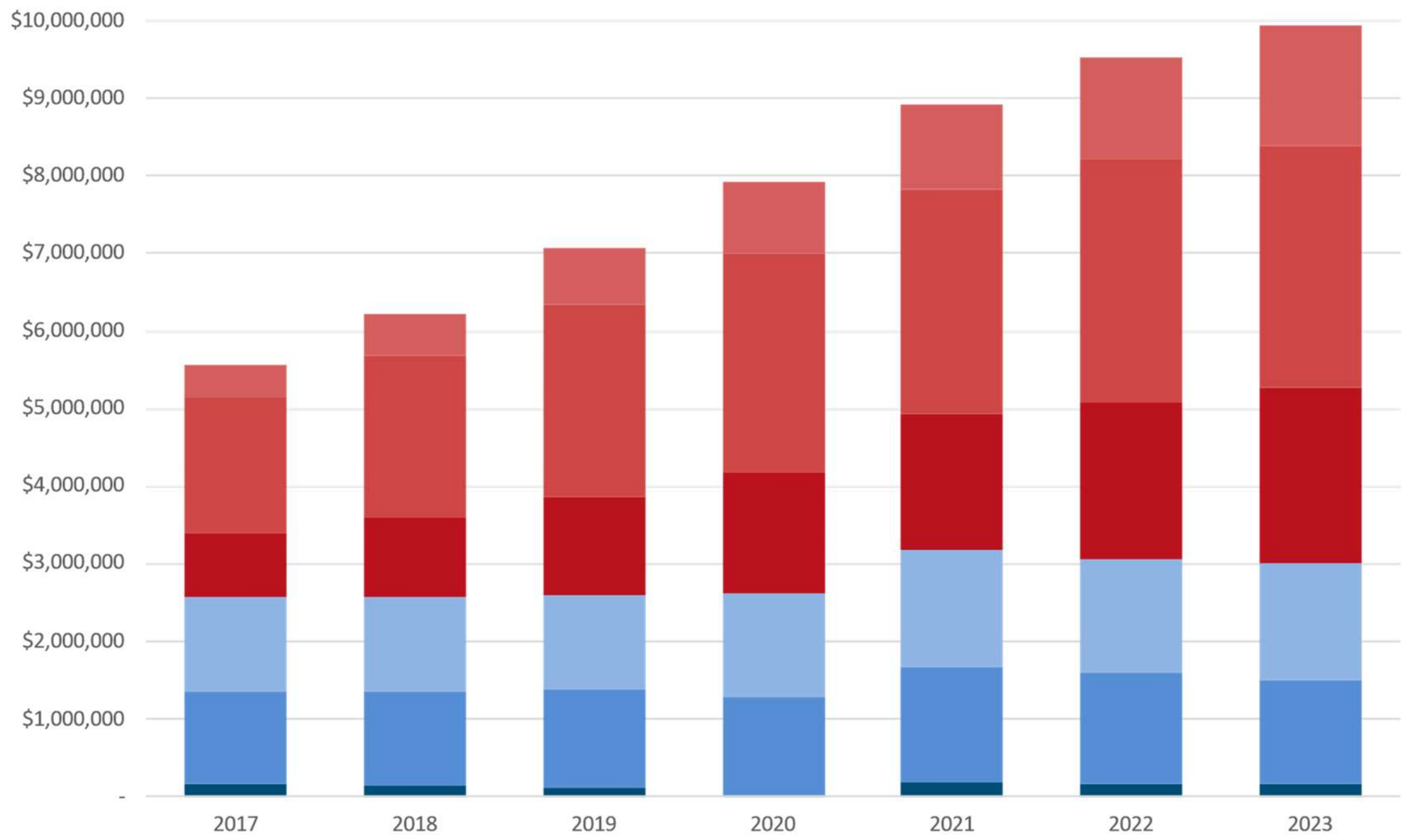
more

Funded Level

4.7%

lower

Pension Payments



	2017	2018	2019	2020	2021	2022	2023
UAL - Safety 2nd	419,403	537,791	717,865	915,312	1,082,812	1,316,917	1,549,858
UAL - Miscellaneous	1,759,914	2,098,803	2,479,328	2,828,711	2,903,218	3,137,154	3,131,488
UAL - Safety 1st	833,853	1,017,949	1,268,454	1,545,867	1,739,130	2,008,376	2,255,922
Normal - Safety 2nd	1,198,920	1,208,049	1,215,543	1,338,099	1,522,126	1,470,195	1,509,078
Normal - Miscellaneous	1,198,076	1,218,864	1,252,744	1,261,314	1,477,345	1,438,044	1,336,803
Normal - Safety 1st	164,858	149,168	129,036	31,438	187,606	155,834	160,245

Annual Pension Payment Increase

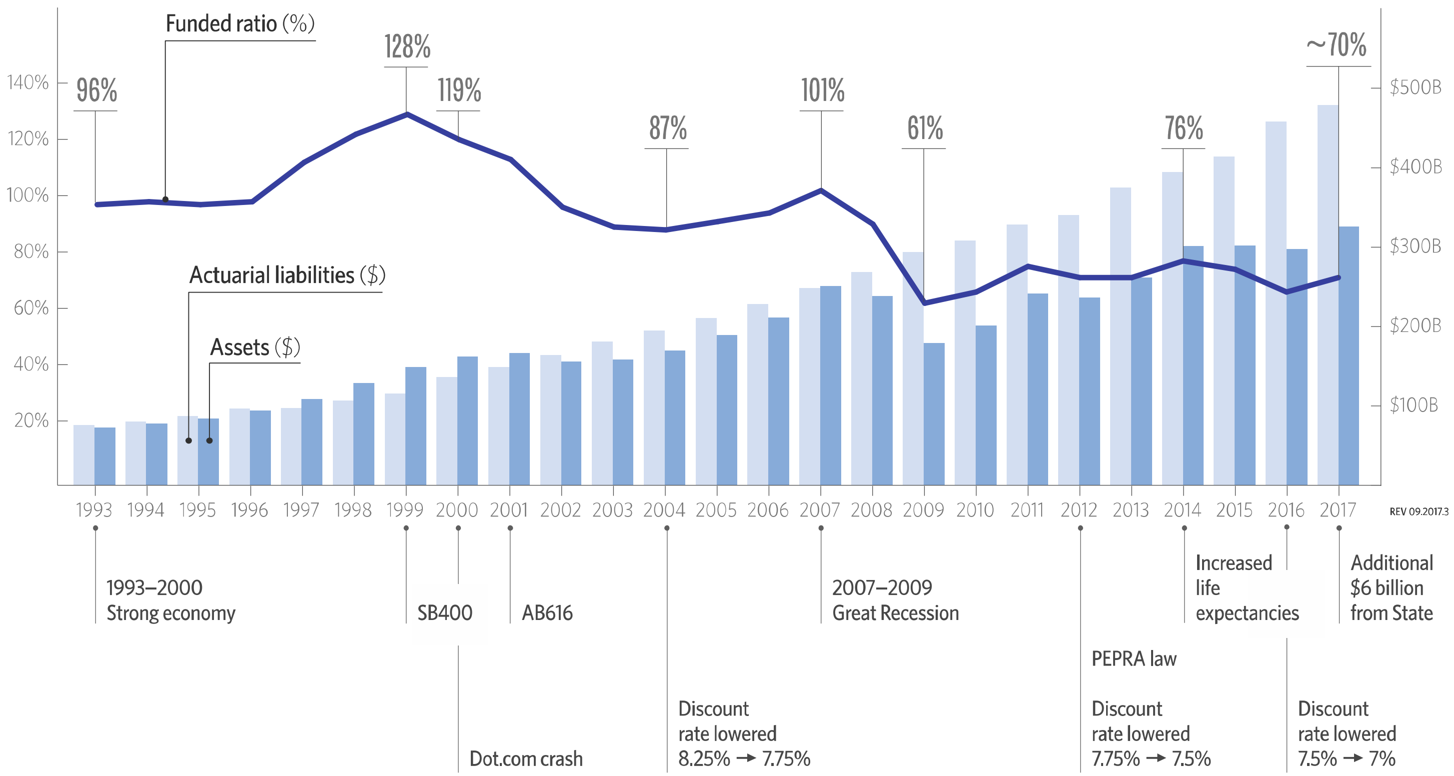
$4.4M

in seven years

UAL as a Percent of Total Payments

2017	2023
54.0%	69.8%

CalPERS History Lesson



1999 – CalPERS 128% funded ("Super Funded" Status)

2000 – SB 400 / AB 616 increased benefits retroactively

2000-02 – dot.com investment losses:
- 2000-01: -7.2%
- 2001-02: -6.1%

Loss of "Super Funded" Status

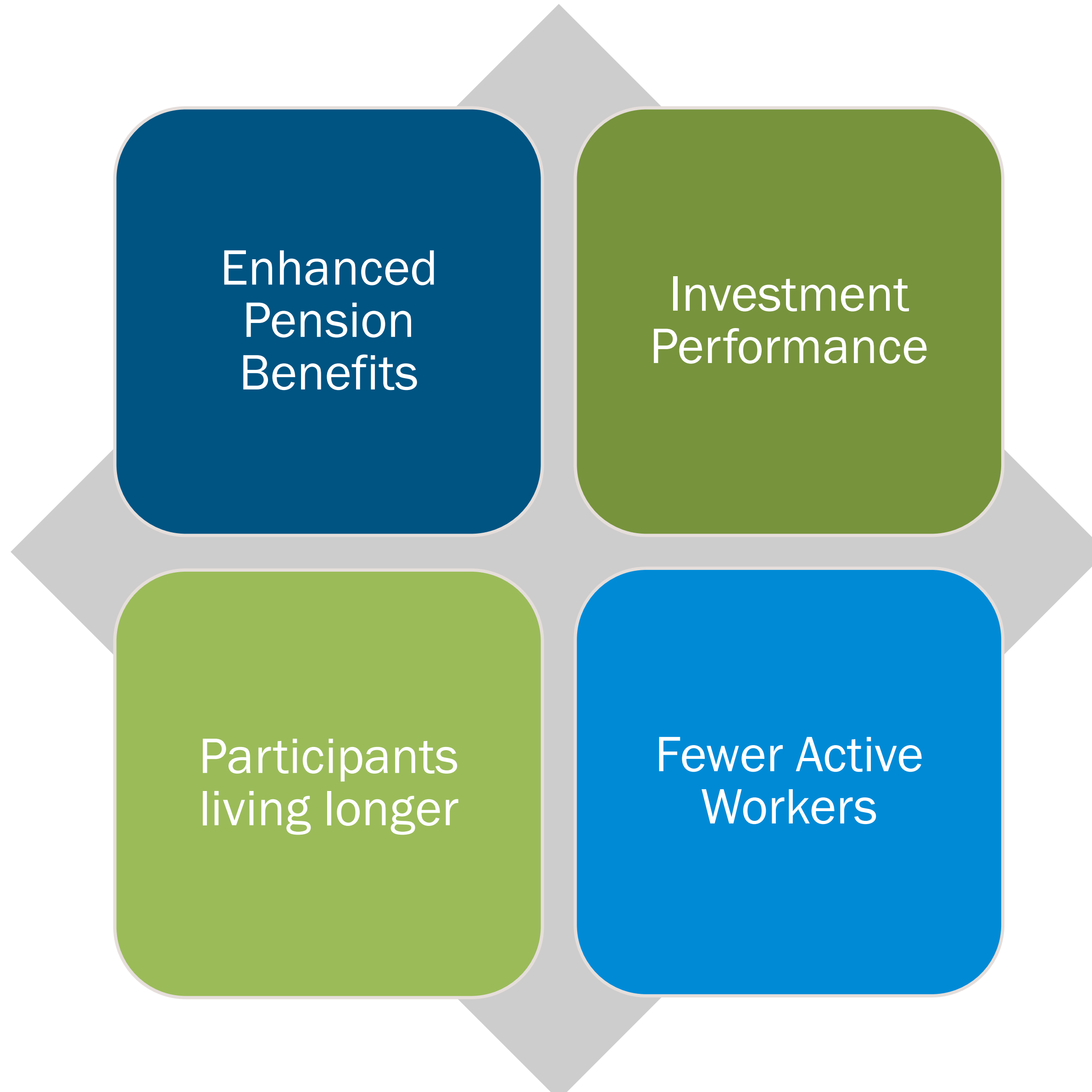
2008-09 – The Great Recession:
- Investment Loss: - 27% ($67 Bn)
- Full impact: - 34.75% (27% + 7.75% discount rate)
- CalPERS 61% funded

2012 – PEPRA reduced benefits for new employees

2020 – CalPERS is 71% funded

Pension Cost Increase Drivers

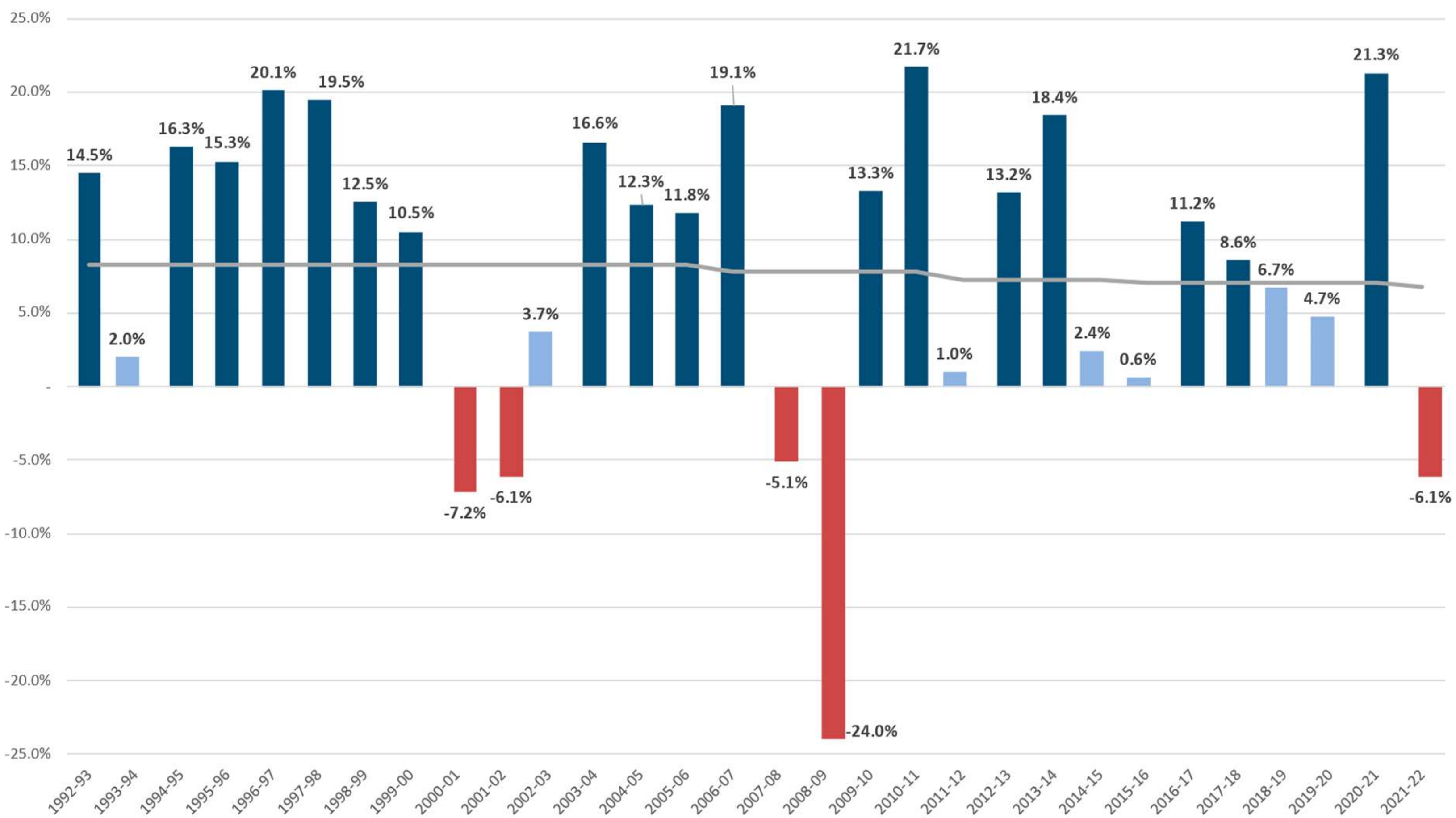
- Enhanced Pension Benefits (SB 400 / AB 616)
- Investment Performance vs Overly Optimistic Return Expectations
- People Living and Drawing Pensions Longer
- Fewer Active Workers for Each Retiree
- CalPERS Assumption Changes
    - Discount rate reduction
    - Actuarial Amortization Policy
    - Mortality rates



Investment Risk and Returns

CalPERS Historical Average Rates of Return through 2021-22:

Past: 5 years – 7.0% 10 years – 8.1% 15 years – 5.9% 20 years – 7.6% 25 years – 7.2%



2050: 55% of pension benefits funded by investment returns

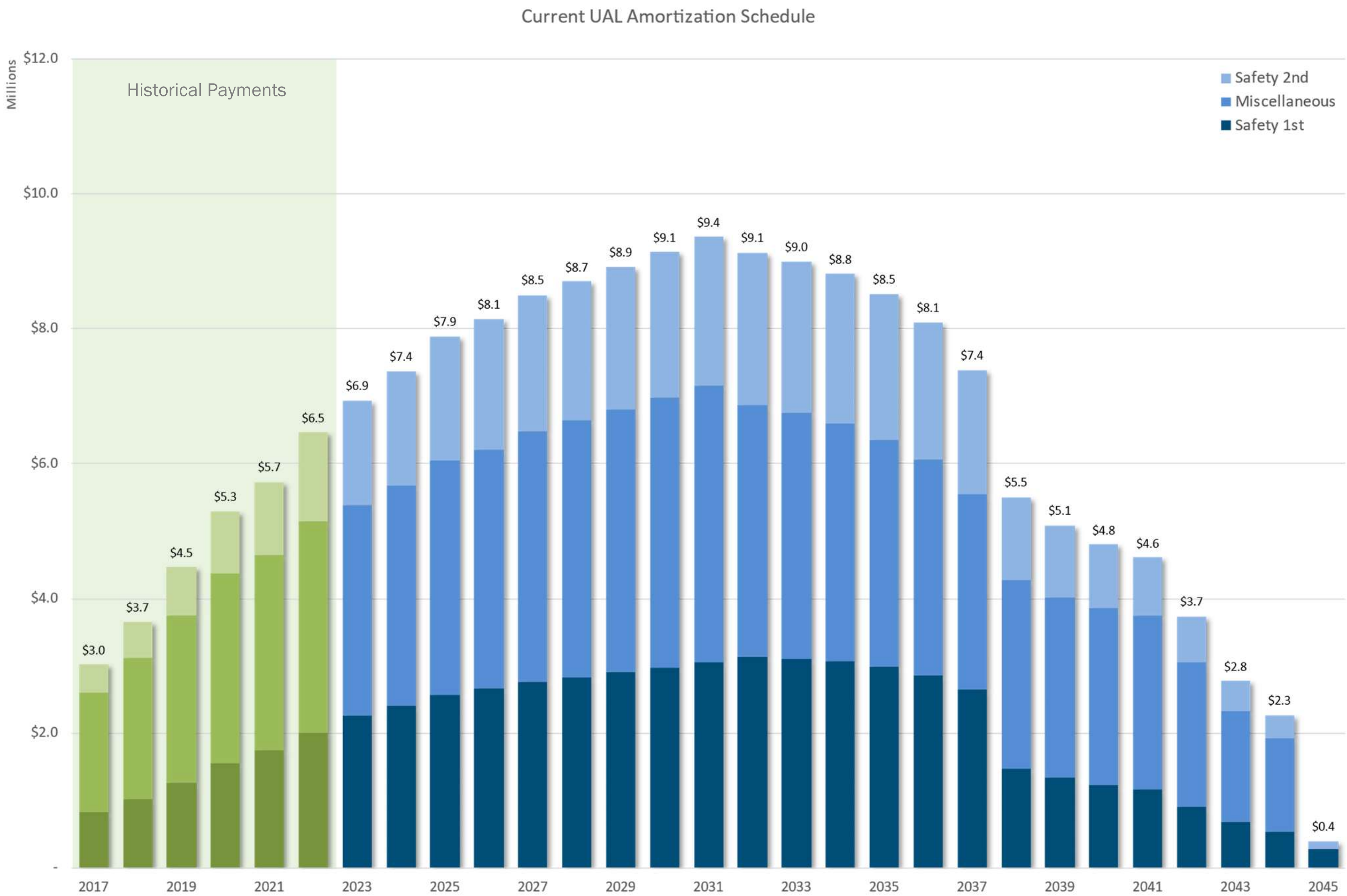
CalPERS manages pension investments

City bears all investment risk

Failure by CalPERS to achieve target investment returns does not relieve City from pension benefit guarantees to employees and retirees

Lower returns => higher UAL and higher pension payments by City

Where Things Currently Stand



06/30/2020 Actuarial Valuation

INCLUDES:

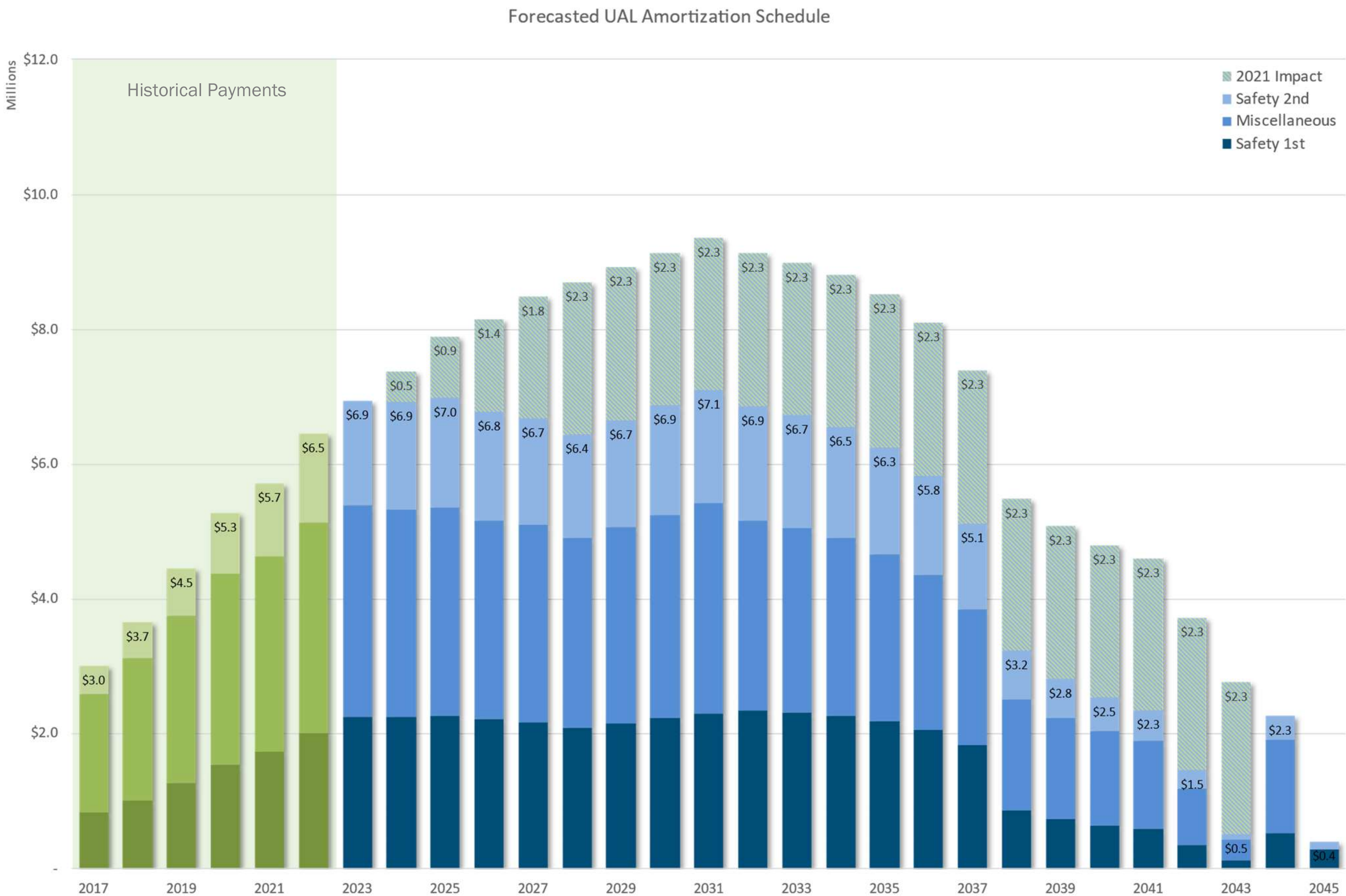
- UAL Payments Only

DOES NOT INCLUDE:

- Misc – Normal Cost (10.9% of salaries)
- Safety 1st – Normal Cost (9.0% of salaries)
- Safety 2nd – Normal Cost (9.0% of salaries)

	As of 2020
Principal	$87.7M
Interest	$68.3M
Total Due	$155.9M

Estimated 2021 Investment Impact



06/30/2020 Actuarial Valuation

INCLUDES:

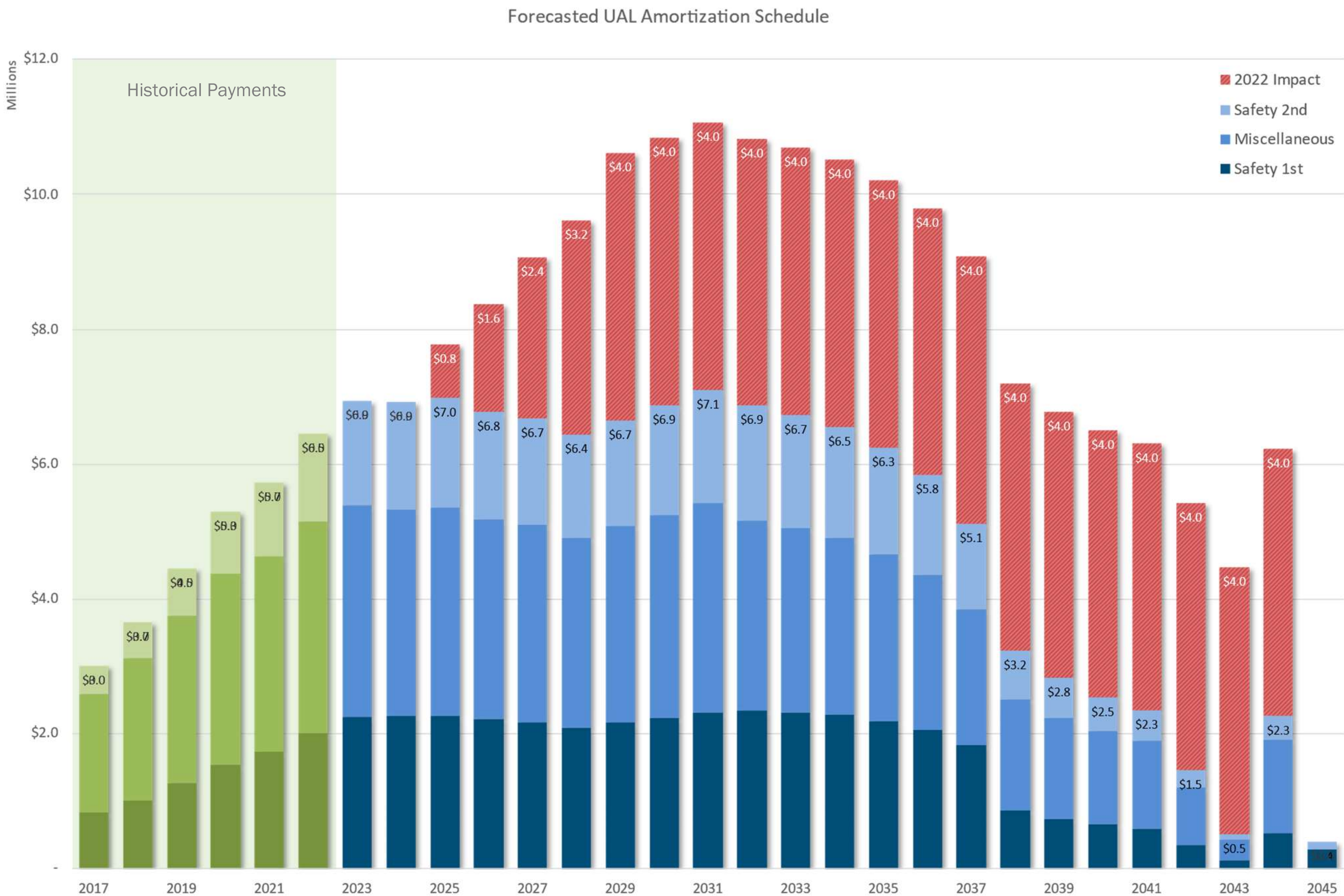
- UAL Payments Only
- Estimated impact of 21.3% Return

DOES NOT INCLUDE:

- Misc – Normal Cost (10.9% of salaries)
- Safety 1st – Normal Cost (9.0% of salaries)
- Safety 2nd – Normal Cost (9.0% of salaries)

	As of 2021
Principal	$69.6M
Interest	$45.6M
Total Due	$115.2M

Estimated 2022 Investment Impact



06/30/2020 Actuarial Valuation

INCLUDES:

- UAL Payments Only
- Estimated impact of 21.3% Return
- Estimated impact of -6.1% Return

DOES NOT INCLUDE:

- Misc – Normal Cost (10.9% of salaries)
- Safety 1st – Normal Cost (9.0% of salaries)
- Safety 2nd – Normal Cost (9.0% of salaries)

	As of 2022
Principal	$101.3M
Interest	$84.4M
Total Due	$185.7M

CalMuni ADVISORS

Pension Strategy Objectives

Pension costs cannot be viewed in a vacuum

Strategy must incorporate reserves, cash flow constraints, policy objectives, and current political dynamics

- Normal Cost - can only be reduced thru labor practices
- UAL Payments – can be reduced thru multiple strategies

Two approaches to pension cost management:

SHORT-TERM CASH FLOW MANAGEMENT

- Achieve budget predictability
- Extend UAL payments over longer term

LONG-TERM COST MANAGEMENT

- Reduce overall interest cost for the City
- Prepay or accelerate UAL payments

Pension Liability Management Policy

The development of a robust Pension Liability Management Policy is one of the key building blocks to maintaining a healthy funding status for the City's pension plans.

- Establishes long-term targets for plan funding levels and a roadmap for annual review and action.
- Provides direction and prioritization for the use of surplus funds for developing, maintaining, and utilizing City reserves.
- Develops a comprehensive waterfall framework for current and future staff to manage reserves for current and future liability management.

The Pension Toolbox

The range of options available to address unfunded liabilities range from incremental items that are reviewed and considered annually, to one-time items that can potentially provide robust impact.

PAY DOWN	REFINANCE	STABILIZE
1. UAL Prepayment • Annual prepayment • From reserves, one-time revenues and fund surpluses • Sale of non-essential assets 2. Fresh Start / Informal Fresh Start 3. New Sources of Revenue	4. Savings from Debt Refundings 5. Capital Financing • From CIP Reserves • Pay-Go Programs 6. Pension Obligation Bonds	7. IRS Designated 115 Trust 8. Self-managed Reserve Fund

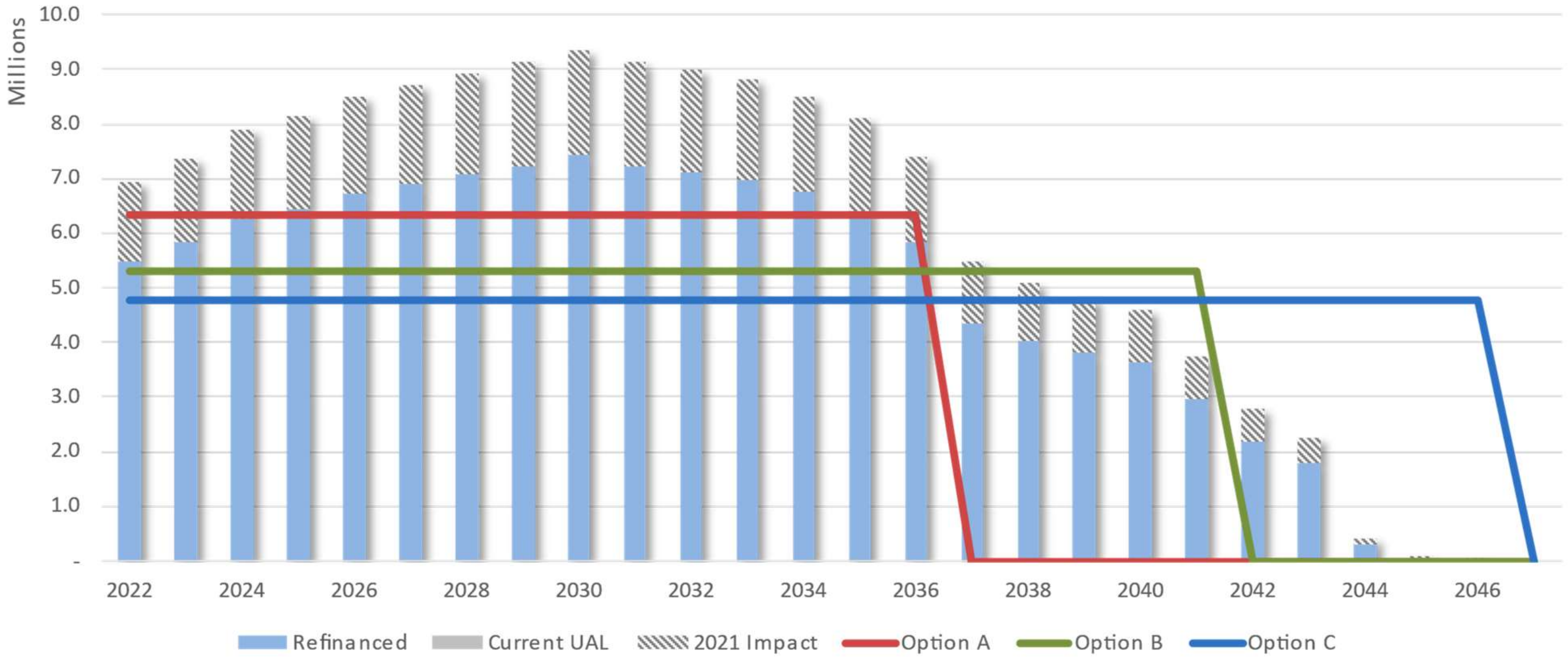
Recent Pension Refinancing Activity

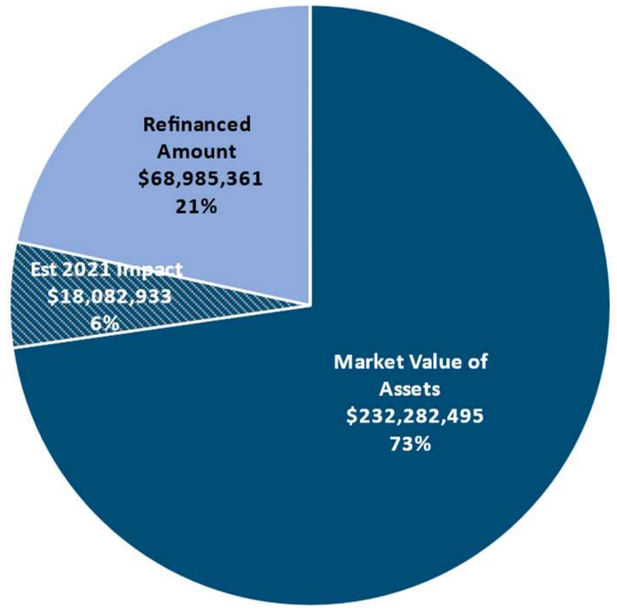
California Municipal Advisors and Weist Law have worked together on 14 recent pension refinancings.

City of Susanville	$10,601,500	Private Placement
City of Arcata	$3,226,000	Private Placement
Calaveras County Water District	$5,665,000	Private Placement
City of Ukiah	$49,875,000	Public Placement
City of Gustine	$2,353,711	Private Placement
San Benito County Water District	$3,016,000	Private Placement
Borrego Springs Fire Protection	$1,874,111	Private Placement
Bonita Sunnyside Fire Protection	$5,127,000	Private Placement
Lake Valley Fire Protection District	$10,952,522	Private Placement
Arcata Fire Protection District	$4,754,000	Private Placement
Ebbetts Pass Fire Protection District	$3,518,000	Private Placement
Oceano Community Services District	$906,000	Private Placement
Rancho Adobe Fire Protection District	$5,610,000	Public Placement
City of Cotati	$4,087,760	Public Placement

☐ *Denotes transactions that have a case study located in the appendix*

Baseline Refinancing Scenarios

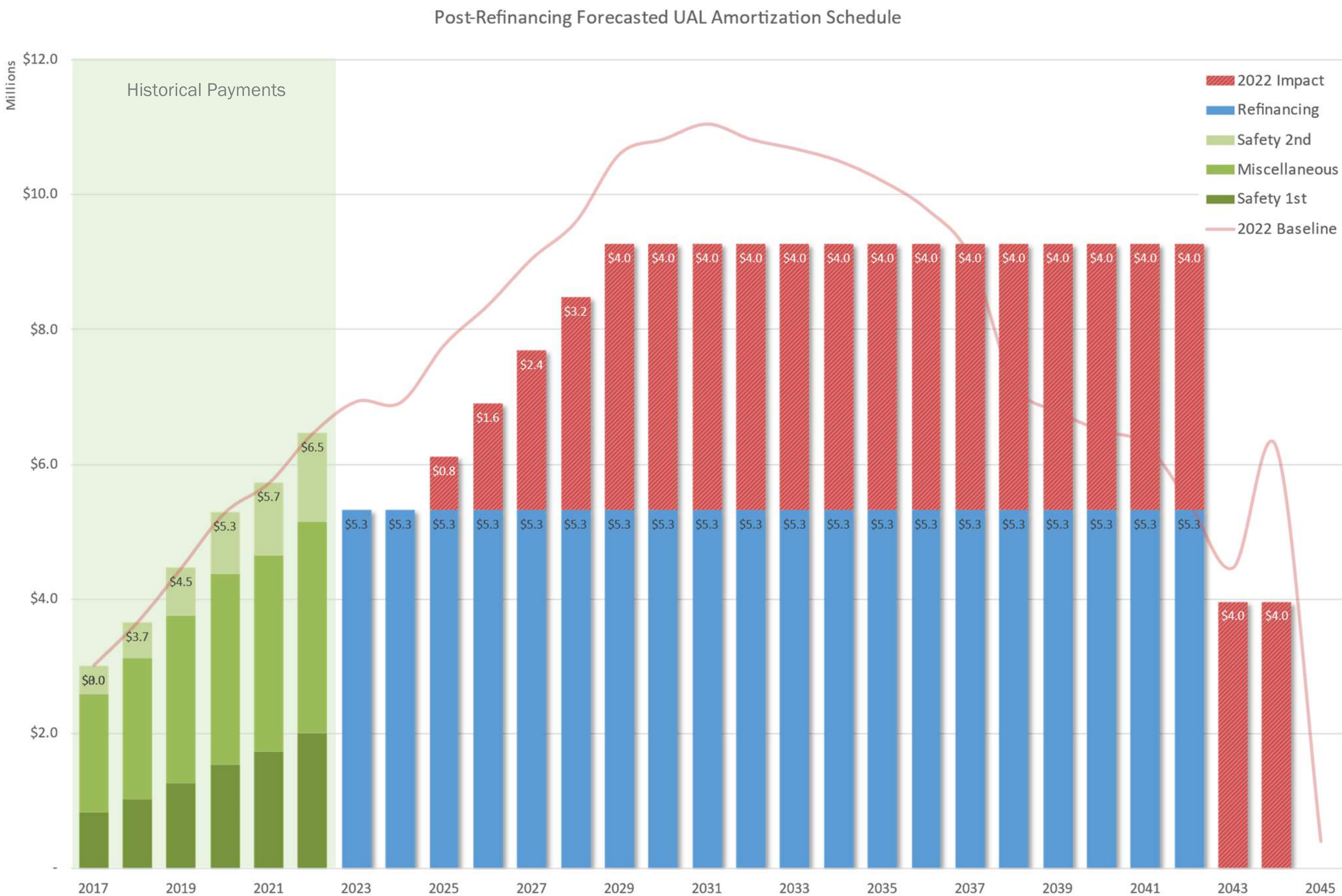




Scenario	Term	% of UAL Refunded	Total Financing Cost	Est Interest Rate	Cash Flow Savings Years 1-10	Cash Flow Savings Years 11-15	Cash Flow Savings Years 16-25	Total
Current CalPERS UAL			$87,068,294	7.00%	$ -	$ -	$ -	$ -
UAL Refinanced (79.23%)			$68,985,361					
A	15 years	79%	($69,185,361)	4.25%	$3,304,200	$9,851,200	$14,781,473	$27,936,873
B	20 years	79%	($69,185,361)	4.50%	$13,435,899	$4,279,642	($1,174,638)	$16,540,903
C	25 years	79%	($69,185,361)	4.75%	$18,756,958	$8,004,384	($23,511,310)	$3,250,031

- Interest Rate estimates are based on current market rates. Actual rates may vary.
- Refinancing amounts include semi-annual loan payments and costs of issuance (estimated at $200,000 for public sale).
- Cash flow savings can be utilized to build up reserves, pay down future UAL increases, set up reserves for future OPEB costs, or any other legal purpose of the City.
- Some or all generated savings can be sequestered into a 115 Trust reserve in order to build resilience.

Post-Refinancing Depiction



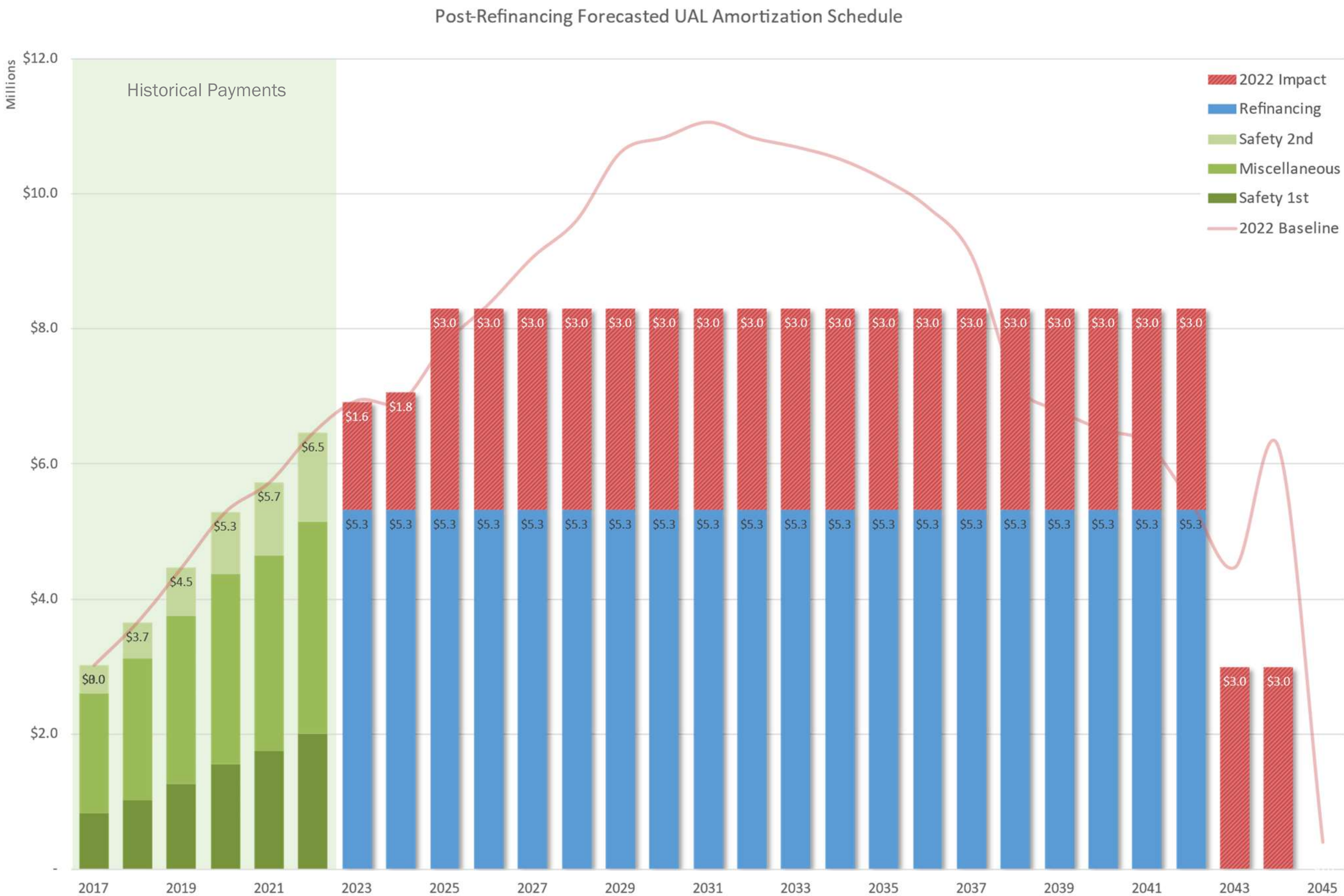
06/30/2020 Actuarial Valuation

INCLUDES:

- UAL Payments Only
- Estimated impact of 21.3% Return
- Estimated impact of -6.1% Return
- 20-year Refinancing

	As of 2022
Principal	$101.3M
Interest	$76.3M
Total Due	$177.6M

Post-Refinancing Depiction with Base Acceleration



06/30/2020 Actuarial Valuation

INCLUDES:

- UAL Payments Only
- Estimated impact of 21.3% Return
- Estimated impact of -6.1% Return
- Base Payment Acceleration
- 20-year Refinancing

	As of 2022
Principal	$101.3M
Interest	$68.2M
Total Due	$169.5M

Next Steps

- Step 1: Pension Liability Management Policy Development
- Step 2: Analyze Initial Pension Liability Management Initiatives
  - Additional Discretionary Payments Strategies and Calculations
- Step 3: Proposed Pension Liability Management Policy & Initiatives
  - Consideration for Adoption by Council
- Step 4: Provide On-Going Pension Liability Management Support
  - Review of Annual CalPERS Valuation Reports
  - Reserve Contribution Calculations
  - Annual Capital Improvement Program Review
  - Additional Discretionary Payments Strategies and Calculations

QUESTIONS?

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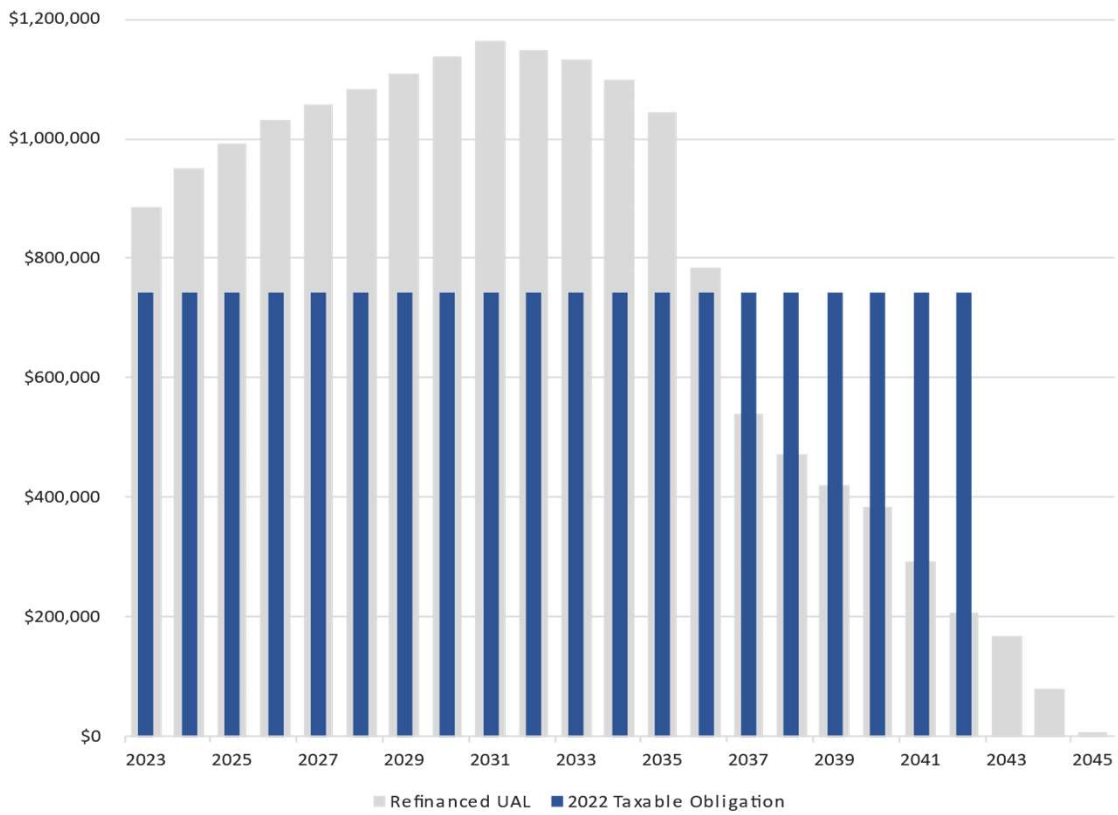
APPENDIX

Case Study: City of Susanville, California

The City of Susanville engaged CalMuni Advisors in order to prepare for a public offering of taxable debt in order to make a large additional discretionary prepayment to CalPERS for their unfunded accrued liability (the "UAL").

Transaction Highlights

For pension debt to be legally financed, the legal structure must either be "validated" through a judicial validation proceeding or some other alternative legal theory arranged. The team at Weist Law filed a validation judgment in the Superior Court of Lassen County. The validation action was then challenged by the Howard Jarvis Taxpayers Association. To defend the validation action through the judicial process could take a year or longer before funding could be approved. During that same time period, interest rates continued to rise due to the lingering effects of Covid-19, significant inflationary pressures, fed rate hikes, and the outbreak of war in Ukraine. Therefore, the team felt it was their fiduciary duty to reconvene with the City Council to discuss the recent market headwinds and generate a strong financing strategy to withstand volatility.



After analyzing all viable options, the team found that it would be most advantageous to the City to restructure the financing by utilizing lease arrangements for a private offering. Lease financings have judicial precedence in California, known as the "Offner-Dean-Rider Lease Exception" to the California Constitutional Debt Limitations. The team reached out to several banks that regularly invest in municipal debt obligations to get their indicative rates. One bank was able to offer a competitive rate of 3.5% for a 20-year term. Council approved the switch from a public offering to a private placement process and accepted the bank term sheet for a 20-year term at a 3.50% rate.

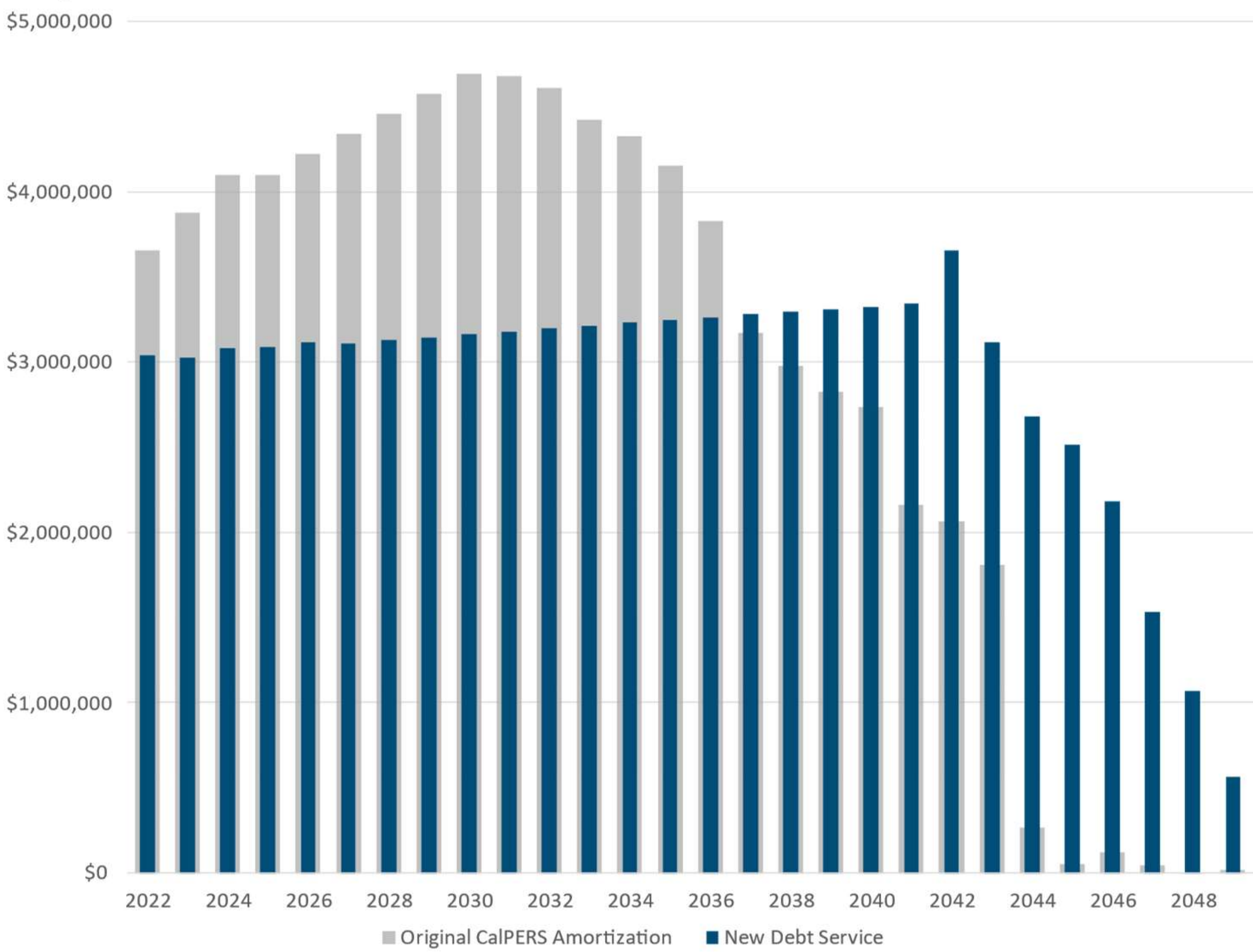
Successful Outcome

- The transaction resulted in total projected cash flow savings to the City of approximately $2,338,712
- Due to an innovative Net Revenue and asset pledge structure, the City was able to achieve a 20-year taxable interest rate of 3.50% (even during a highly inflationary period).
- The Financing Team was able to achieve a favorable interest rate in the midst of rapidly rising interest rates (rates had increased to over 4.40% at the time) and quickly "pivot" the financing structure in the best interests of the client–all within a span of less than 60 days. This "pivot" resulted in additional savings to the City of approximately $1,000,000 over what would have been achievable through a private placement

Case Study: City of Ukiah, California

City of Ukiah

The City of Ukiah, California issued $49,875,000 2020 Taxable Lease Revenue Bonds (CalPERS Prepayment Project). The transaction was completed to refinance the City's outstanding unfunded accrued liability (UAL) associated with their CalPERS "classic" Miscellaneous, Fire Safety and Police Safety pension plans.



Transaction Highlights

Due to the accumulation of amortizing UAL bases over the years, the City was facing steeply increasing UAL cost curves, with the UAL Payments approximately doubling from FY 2020 to FY 2032-33. Weist Law worked closely with the City of Ukiah to spearhead a complex legal and financing strategy culminating in the City's pension plan funded status rising from approximately 70% funded to over 93% funded.

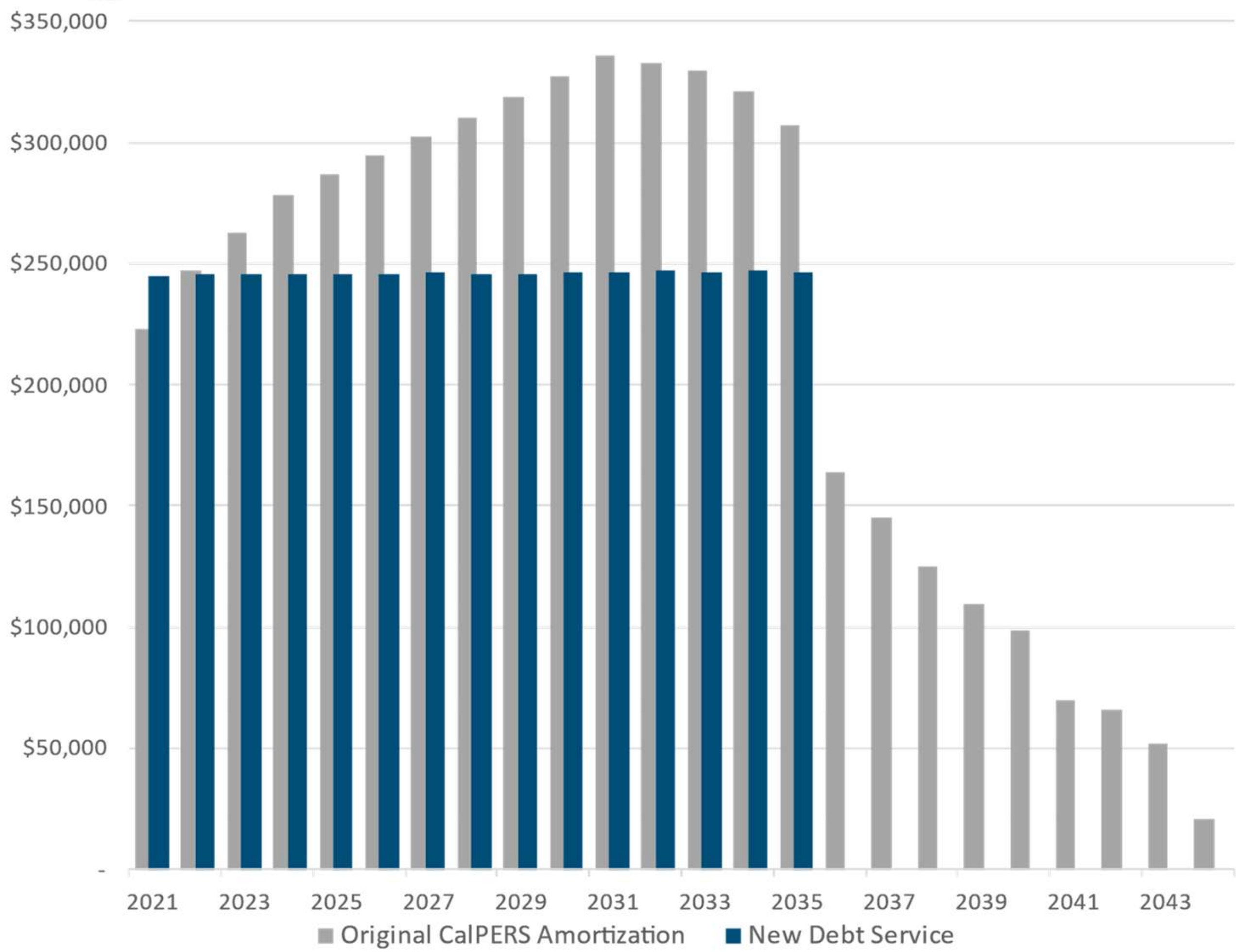
Projected savings over the first 15 years is projected to be greater than $24 million, which provided much needed budget resiliency due to the uncertainties surrounding Covid-19 impacts and allowed the City to more securely address uncertainties related to future CalPERS performance.

Successful Outcome

- By reshaping the escalating UAL payments to near-level debt service payments, the transaction provided the City with budget predictability and resiliency over the 29-year term of the Bonds.
- The Bonds received an S&P rating of A+ and were issued without a reserve fund, which created further fiscal efficiencies.
- The City was able to recognize savings and utilize them to set aside funds to pay down future UAL bases and maintain their CalPERS funding targets.

Case Study: San Benito County Water District

The San Benito County Water District issued $3,016,000 Series 2021 Taxable Revenue Obligations (CalPERS UAL Prepayment Project), issued to refinance the District's outstanding unfunded accrued liability (UAL) associated with their CalPERS "classic" pension plans.



Transaction Highlights

Weist Law, as Bond Counsel, and CalMuni Advisors, as Municipal Advisor, worked with the San Benito County Water District to provide in-depth analysis of the District's pension plans and the various mitigation strategies for each of the plans. The comprehensive study sessions evolved into discussion of a refinancing of outstanding UAL as one of the mitigation strategies to reverse the trend of escalating year-over-year payments being made to CalPERS.

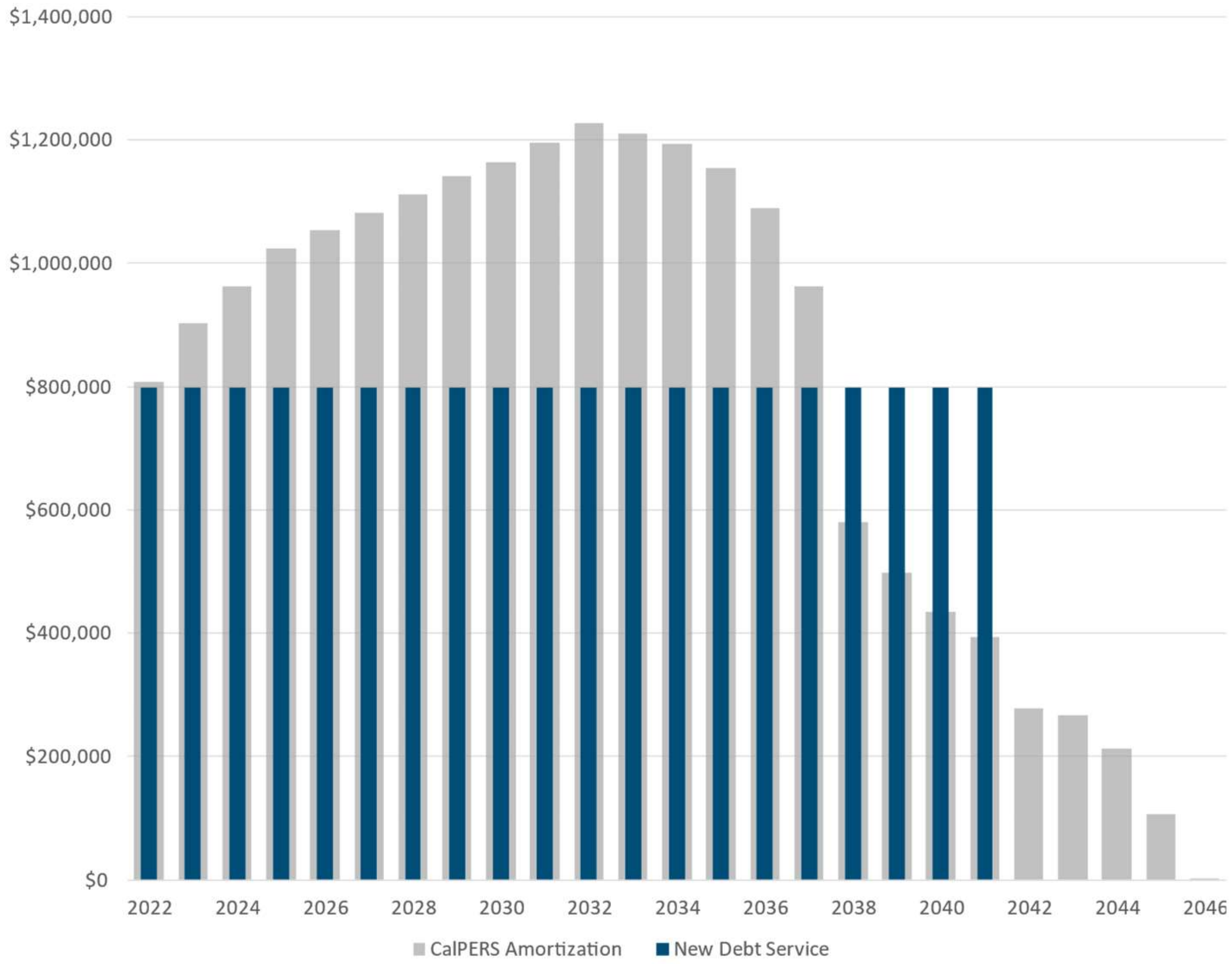
Based on the analysis, projected savings over the first 15 years was anticipated to be greater than $750,000, providing much needed budget resiliency and allowed the District to more securely address uncertainties related to future CalPERS performance.

Successful Outcome

- The transaction resulted in total cash flow savings to the District of approximately $1,595,000 and as importantly, reshaped escalating payments to level debt service payments over the 15-year term of the 2021 Obligations.
- Due to a unique Net Revenue pledge structure, the District was able to achieve a 15-year taxable interest rate of 2.94% which equates to a 2.05% tax-exempt rate with total costs of issuance under $70,000.

Case Study: Lake Valley Fire Protection District

Lake Valley Fire Protection District issued $10,952,522 Series 2021 Taxable Revenue Obligations (CalPERS UAL Prepayment Project). The transaction was completed to refinance the District's outstanding unfunded accrued liability (UAL) associated with their CalPERS "classic" Miscellaneous and Fire Safety Pension Plans.



Transaction Highlights

Due to the accumulation of UAL bases over the years, the District was facing steeply increasing UAL cost curves, with the UAL payments approximately doubling from FY 2020 to FY 2032. This UAL growth was recognized as a growing concern to the District as it would increasingly impact the General Fund.

CalMuni Advisors and Weist Law worked with the District to provide in-depth analyses of the District's pension plans and the various mitigation strategies for each plan. The study sessions resulted in a plan to refinance the outstanding UAL of the classic plans in order to provide a 20-year level debt service thus providing budget predictability while also providing cash flow savings to the District.

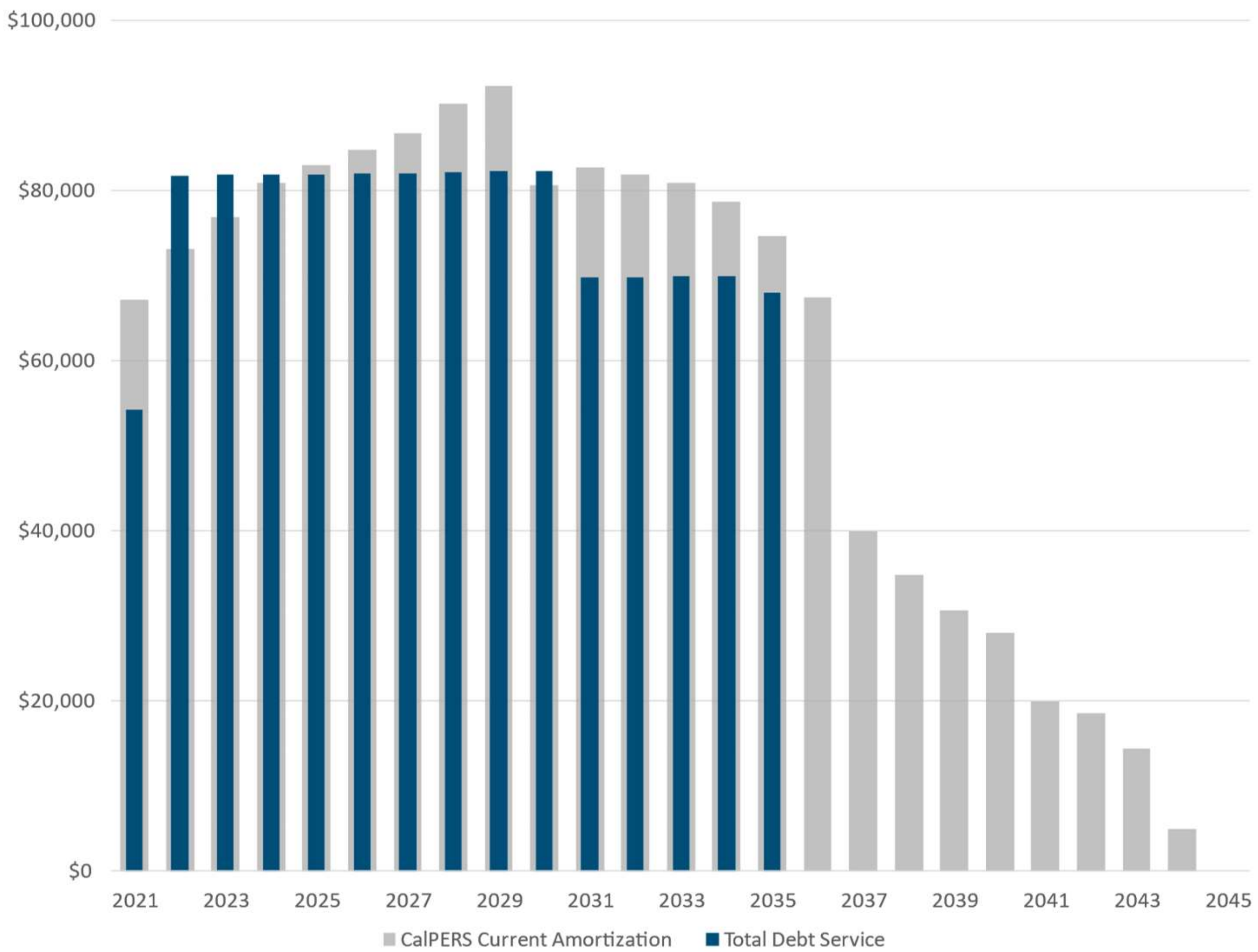
Successful Outcome

- The transaction resulted in total cash flow savings to the District of approximately $4,255,811 and as importantly, reshaped escalating payments to level debt service payments over the 20-year term of the 2021 Obligations.

- With a taxable 4.00% interest rate locked in, the District is positioned to benefit from savings that will allow it to more proactively manage future unfunded liabilities and maintain a healthy funding status of its pension plans.

Case Study: Oceano Community Services District

Oceano Community Services District issued $906,000 Series 2021 Taxable Revenue Obligations (CalPERS UAL Prepayment Project). The transaction was completed to refinance the District's outstanding unfunded accrued liability (UAL) associated with their CalPERS "classic" Miscellaneous and Fire Safety Pension Plans.



Transaction Highlights

The refinancing transaction was successfully structured to mimic a standard Net Revenue pledge structure with industry standard rate covenants and parity debt provisions (unlike pension obligation bonds which do not have parity bond tests, etc., which can make future financings very difficult and/or very expensive). The effect of the Refinancing was to (i) allow UAL pension costs to be financed at best possible interest rates, (ii) allow for future financings at best terms, (iii) move the financed UAL pension cost from maintenance and operation expenses to debt service on parity with all other outstanding parity debt, and (iv) automatically increase the District's debt service coverage ratio (because pension costs are treated as M&O, but when financed are moved "below the line" to debt service secured by Net Revenues).

Successful Outcome

- The transaction resulted in total cash flow savings to the District of approximately $334,000 and as importantly, reshaped escalating payments to level debt service payments over the 15-year term of the 2021 Obligations.

- Due to a unique Net Revenue pledge structure, the District was able to achieve a 15-year taxable interest rate of 3.5% which equates to a 2.3% tax-exempt rate with total costs of issuance of less than $76,000.

Next Steps in a Typical Process

Assess Current CalPERS Reports

1 – 2 weeks*

- Determine current UAL payment requirements
- Assess Funding Percent Status
- Review alternative options available through CalPERS

Pension Liability Management Meetings

1 – 2 months*

- Multi-step effort for staff and Council
- Education on CalPERS framework, cost drivers, and current approach.
- Overview of UAL funding strategies

Adopt Pension Liability Management Policy

1 month*

- Based on Pension Liability Management Meetings.
- Draft Pension Management policy that meets the unique fiscal needs of the City.
- Presentation to Council for adoption.

Assess Refinancing Strategies

2 - 3 months*

- At the direction of the Council & Staff, CalMuni will perform various analyses on refinancing strategies.
- Council determination on whether a refinancing is appropriate for City.
- Initiate and complete UAL refinancing if appropriate.

Annual Pension Assessment

Ongoing*

- During each year's budget cycle, perform annual pension performance assessment.
- Determine future funded percent based on CalPERS investment performance and actuarial changes.
- Implement policy strategies to maintain funded percent and healthy reserves.

** Timeline is indicative only and can be slowed or accelerated based upon need and objectives of the City.*

Refunding Considerations – Benefits & Risks

Benefits

- Enhanced budget predictability from new "flattened" repayment structure
- Estimated near-term cashflow savings from lower interest rate
- Present value (PV) savings achieved if CalPERS earns more than the refunding interest rate
- Increased "funded status" of City's retirement plan
- Cash flow savings can be utilized to build up reserves, pay down future UAL increases, set up reserves for future OPEB costs, or any other legal purpose of the City
- Interest rates are presently at all-time lows

Risks

- CalPERS Reinvestment Risk: CalPERS will have more money to invest
  - Same for any UAL prepayment
- PV Savings not guaranteed: CalPERS has to earn more than the refunding interest rate
  - Easier to achieve than earning CalPERS' own 7% discount rate
- Listed as "debt" on City's financial statements
  - UAL is also shown as liability on financial statements
- For asset-secured structures, City's owned assets may be required as collateral

The Sale Process - Options

Selecting the method of sale for a transaction is determined based upon a range of variables by the Issuer and Financing Team in order to ensure that the needs of the Issuer are met and the target outcome is achieved.

	Public Sale	Private Placement
Transaction Size	Flexible	Up to $30M
Pricing	Lower Rates Higher Costs of Issuance	Higher Rates Lower Costs of Issuance
Time to Close	3+ Months	2+ Months
Issuer Involvement Level	High	Low to Moderate
Structure	Standardized	More Flexible
Term	Up to 40 years; typically 30 years	Up to 20 years
Due Diligence	Issuer, counsel, Rating City	Bank
Prepayment Flexibility	Limited without cost	Various Options
Structure	Rigid and Standardized	More Flexible
Credit Rating	Required	Not Required
Debt Service Reserve	More Often	Less Often
Continuing Disclosure Requirements	Strict	More Flexible Options

The Sale Process - Timeline

The sale process varies depending on which approach an issuer selects.

- The public sale process is longer and more complex it can often lead to more competitive pricing
- The private placement process is simpler but reduces the number of potential investors often resulting in higher rates.

Public Sale 90-120 days	Private Placement 60-90 days
Select Financing Team	Select Financing Team
Develop plan of finance	Develop plan of finance
Draft legal documents	Draft legal documents
Draft investor disclosure (Official Statement)	Prepare and distribute Request for Proposals to lenders
Obtain credit rating and bond insurance (as needed)	Receive proposals and lock interest rate
Obtain Council approval	Complete lender due diligence & obtain credit approval
Market bonds to investor community	Obtain Council approval
Collect orders and set interest rates	Close transaction and transfer funds to CalPERS
Close transaction and transfer funds to CalPERS	Make timely payments and provide ongoing disclosure
Make timely payments and provide ongoing disclosure	Keep records
Keep records	