From:	John Nachtigall
To:	_CityCouncilListPublic
Cc:	Mazyck, Jan
Subject:	[EXTERNAL] Recent Discussion on Pension Obligation Bonds
Date:	Wednesday, July 21, 2021 12:35:34 PM
Attachments:	image.png

Hello

I am a citizen of Santa Rosa and have been for the last 10 years. I am writing in regards to the recent discussion regarding pension obligation bonds (POBs). I would urge the council to reject this idea. POBs are not a "refinance" of debt, they are a gamble. Specifically they are a gamble that the return on the invested money will be larger than the interest rate on the loan.

It is true that the unfunded liability for Santa Rosa pensions (estimated at 110 million) is set. While CAPERs returns may cause it to fluctuate somewhat, there is no doubt that this debt is real and will have a very real impact on the Santa Rosa budget. However, as my father told me, when you find yourself in a hole, stop digging. By issuing POBs the city will be borrowing more money to make a bet that the investment returns will outpace the discount rate that CALPERs charges. While that may seem like a "good bet", it is still a bet. At no point should a government be gambling with its budget.

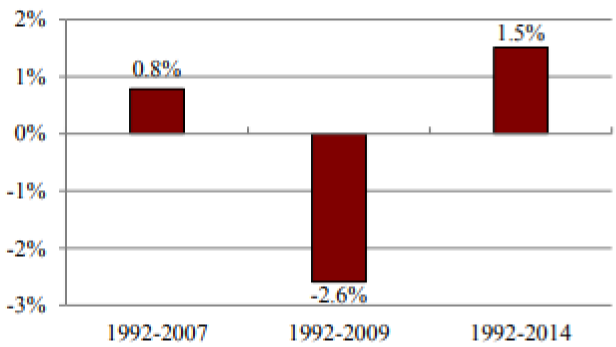
I have no doubt about Ms Mazyck's abilities, knowledge, and sincerity (she is copied on this email). Some of the risks of POBs were given, however, a full discussion of the risks and more importantly the historical performance of POBs was not presented.

I would point the council to an excellent non-partisan examination of the subject by the Center for Retirement Research at Boston College.

http://crr.bc.edu/wp-content/uploads/2014/07/slp_40.pdf

While the entire issue is examined, Figure 4 (below) provides a summary. Depending on the time period examined the POBs actual average rate of return was between 1.5 to -2.6%. It is true that some of the bonds have yielded positive results, but the risk of additional debt is not offset by amazing returns, these are paltry numbers.

Figure 4. Average Internal Rate of Return on Pension Obligation Bonds, 1992-2007, 1992-2009, and 1992-2014



Source: See Figure 3.

I have avoided mentioning individual case studies (like Detroit) because I believe the combined numbers provide a better understanding of the issue. But I would be remiss in mentioning that there are individual cases where these bonds have not just added to the debt burden, but bankrupted the city. That is a tremendous risk for a hoped 1% IRR return.

I am sure you will be told that "this time is different". In fact the presentation included a slide declaring these would be POB 2.0 bonds that are "better" than the previous incarnations. And I am sure that many consultants will be happy to run "stress tests" to show that even if 2008 happened again, you should issue these bonds (and invest with the consultants). I would remind you that every city before has heard those same assurances. Every city has run stress tests and been told the risk is small to negligible. As an example, the disastrous Detroit POBs were given the bond issuance of the year award because they were thought of as so clever.

I certainly understand the desire to "do something" to reduce the burden of pensions on city finances. But POBs, while a tempting alternative, are just a siren song that increases the risk to city finances without providing a commensurate possible benefit. I urge you to learn from history rather than repeat it.

Thank you for your time

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