



HISTORIC
FRANKLIN
TENNESSEE

03 FINANCE
10/23/13

MEMORANDUM

October 21, 2013

To: Board of Mayor and Aldermen

From: Eric Stuckey, City Administrator
Russell Truell, ACA Finance

Subject: Pension Obligation Bonds – Path to Final Approval

Purpose

The purpose of this memorandum is to provide information to the Board of Mayor and Aldermen (BOMA) for consideration of a final resolution to issue pension obligation bonds and establishment of a public hearing.

Background

In January of this year, the financial advisor to our Pension Plan initiated a discussion about the issuance of pension bonds. Through the year, staff has collected information about the subject and asked to be included in Private Chapter 467, passed by the Legislature in this year's term. The legislation allows certain cities to issue pension obligation bonds and sets a high threshold in financial condition to be able to do so. The City of Franklin fits that description.

Having advised against issuing pensions bonds for many years, both Dahab Associates, our pension advisor and Public Financial Management (PFM), our debt advisor, have concluded that it may be advantageous to issue such bonds given current market circumstances. Those circumstances include current low interest rates for municipal debt; rising interest rates for bonds and other investments; changes in Government Accounting Standard Board (GASB) reporting rules that now require unfunded pension liabilities to be included on the balance sheet in future financial statements; the announcement by Moody's rating services that they will use a stricter standard for calculating unfunded liabilities than that of the GASB, and the rating agencies' stated policy that unfunded pension liabilities will be considered as debt when determining a municipality's bond rating.

After several discussions among the Pension Committee, a proposal to issue up to \$10 million in pension obligation bonds was unanimously approved at the August meeting. The Budget and Finance Committee reviewed some of the material at their August 25 meeting, and forwarded the issue, without a recommendation, for discussion to the BOMA work session. The Board of Mayor & Aldermen approved an initial resolution at the September 24 meeting, and publication of the resolution appeared in the Williamson Herald newspaper on October 3. As of this date, there have been no phone calls, messages, or other communication from citizens regarding the resolution.

In order satisfy the State legislation, one of two paths must be followed in order to finalize the approval process. The City must choose between option 1, an approval process through the Comptroller's office followed by approval from the State Funding Board, or option 2, a detailed presentation to the Board of Mayor & Aldermen followed by a public hearing.

From the time legislation was adopted, City staff considered the Comptroller/State Funding Board option as the more rigorous path and had planned to follow that procedure. Staff also planned to execute the sale of the bonds no later than the first week in December, in order to take advantage of current market rates and to combine with our other pending bond issue. Unfortunately, it is the consensus of our financial advisor, bond counsel, and City staff that there will not be sufficient time to submit our plan to the Comptroller, schedule a meeting with the State Funding Board, receive their response, meet with the rating agencies and still price the bonds before yearend. We



HISTORIC
FRANKLIN
TENNESSEE

MEMORANDUM

could delay the sale of the bonds until 2014, but we would lose the cost savings of issuing the pension bonds with our capital improvement bonds; we would also run the risk of higher interest rates in the months ahead. Because we would be the first City to follow the Comptroller/Funding Board option, there is no precedent for us to use to determine how much time the process would require.

For the reasons listed above, City staff now recommends that we follow the stipulations of option 2, which would require a detailed presentation to the Board, followed by a public hearing that would allow citizens to express their support or concerns about moving forward with this issue. An outline of the presentation is attached to this memo.

Financial Impact

The financial impact of issuing pension bonds is impossible to determine with precision. However, PFM reports that bonds with a final maturity of ten years could be issued at an interest rate of approximately 3.05%. Dahab Associates reports that the best estimate of the earnings on our pension investment would be a range of 5% to 8%, on average, over that period. That estimate is in line with the earnings on the Pension Plan over the last fifteen years. If our advisors are correct, the City would benefit by the differential between the two rates.

The City would also benefit by reducing the unfunded liability more quickly than is currently formulated in our actuarially required contributions from operating budgets. Our actuarial firm has estimated that we could reduce contributions by \$79,000 for each \$1 million of additional investment in the pension fund. Those savings would be used to offset the additional debt service created by the pension bonds.

Recommendations

Staff recommends that the Committee support Option 2 of the State legislation and advise the City Administrator to give notice of a public hearing on November 26.