California Debt and Investment Advisory Commission

Webinar Frequently Asked Questions
Municipal Debt Issuance Fundamentals Mini-Series
September 9 and 16, 2020

1. Green Bonds – What are green bonds and how are they different from regular bonds?

Green Bonds are bonds that specifically finance climate change resilient projects or other environmentally beneficial projects. The process for issuing Green Bonds is generally the same as issuing other municipal bonds, however, there are a few additional steps that market participants recommend issuers follow to attract socially conscious investors. The "green" designation on a traditional water or waste management project could potentially attract new investors enlarging the investor base for the issuer. Purchasers of Green Bonds typically require the issuer to specify the environmental benefits of the completed or proposed projects and provide periodic updates of these benefits before and after project completion since they may be purchasing Green Bonds to satisfy specific investment policy goals such as Environmental, Social and Governance (ESG) objectives or Socially Responsible Investment (SRI) categories. Issuers are encouraged to describe the internal procedures used to identify, evaluate and select Green Projects, in addition to the standard "use of bond proceeds" and "project description" sections in the official statements used to sell the Green Bonds. By tracking the proceeds of Green Bonds in a separate portfolio or sub-portfolio to ensure the flow of funds to Green Projects, issuers can facilitate reporting practices and provide assurance of the use of Green Bond proceeds. Periodic Green Project updates are recommended to continue until all the bond proceeds are allocated. This type of environmental performance tracking and reporting is considered voluntary and does not fall under the continuing disclosure regulations of the Securities and Exchange Commission (SEC). Green Bond offerings are labeled as such to allow investors to purchase bonds which finance environmentally beneficial projects therefore sufficient facts must be disclosed so that an informed investment decision can be made and for which any misleading statements may result in an enforcement action by the SEC.

Resources for Green Bonds

- CDIAC produced a three-part webinar called "Green Bonds in the Golden State: A Practical Path for Issuers" that provides practical guidance and elaborates on risks and benefits of a green bond issuance. https://www.treasurer.ca.gov/cdiac/webinars/2019/greenbonds/description.asp?hss_channel=tw-2321551999
- CDIAC's Issue Brief: Green Bonds: https://www.treasurer.ca.gov/cdiac/publications/1409.pdf
- STO/CDIAC's "Growing the U.S. Green Bond Market" and green bonds resources:

https://www.treasurer.ca.gov/greenbonds/resources.asp
- ClimateBonds.net "Growing green bond markets: The development of taxonomies to identify green assets": https://www.climatebonds.net/files/reports/policy_taxonomy_briefing_conference.pdf
- ClimateBonds.net "Post-Issuance Reporting in the Green Bond Market": https://www.climatebonds.net/files/reports/cbi_post-issuance-reporting_032019_web.pdf

2. Disclosure – What disclosure obligations do issuers have?

Municipal issuers have a legal responsibility to protect from making untrue statements of material facts or omissions of material facts in both primary offering materials (Official Statements) and when providing additional information after the debt has been issued (annual reports and material event notices). If the issuer has included certain financial information in its OS it must take the appropriate steps to see that this information is updated and reported annually. Municipal issuers are subject to the federal anti-fraud provisions contained in SEC Rule 10b-5 as adopted by the SEC under Section 10(b) of the Securities Exchange Act of 1934. Issuers should establish disclosure policies, which provide specific guidance on who, how, and when the issuer will provide ongoing disclosures as required by SEC Rule 15c2-12. Both the annual report and any event notices are required to be filed in searchable PDF format through the Electronic Municipal Market Access website maintained by the Municipal Securities Rulemaking Board. The annual report has two parts: (1) the issuer's most recent audited financial statements, and (2) "financial information and operating data" for the issuer for the prior fiscal year of the type contained in the final OS, as specified in the continuing disclosure undertaking (CDU) document. The description in any CDU of other financial information and operating data to be provided should be specific and updated annually as agreed to in the CDU.

Resources for Disclosure
- California Debt Financing Guide, section i.5.1.2 Disclosure Policies, section 6.3.3 Disclosure Standards and Guidance, section 8.4 Continuing Disclosure: https://www.treasurer.ca.gov/cdiac/debtpubs/financing-guide.pdf
- Government Finance Officers Association, "Disclosure and Federal Regulation of the Market for Municipal Securities": https://www.gfoa.org/materials/disclosure-and-federal-regulation-of-the-market-for
- National Federation of Municipal Analysts, "Disclosure Guidelines": https://www.nfma.org/disclosure-guidelines

3. Pension Obligation Bonds – Can you provide a general overview of pension obligation bonds in today's market? What are the risks?

Public agencies issue pension obligation bonds (POBs) to make a payment to the public agency's retirement system (a self-managed system, a group system, the California Public Employees' Retirement System (CalPERS) or the California State Teachers' Retirement System (CalSTRS) to satisfy an obligation to make payment to the system. The pension obligation funded can be the public agency's required payments for the current fiscal year, the public agency's unfunded accrued actuarial liability (UAAL) or both. Pension obligation financings are generally structured with an issuance by the public agency of a note payable to the retirement system. The note is then refunded with POBs issued under Local Agency Refunding Law. The retirement system can invest in a broad range of investments, including equity securities. Because of limitations on the ability to fund working capital, POBs are generally issued as taxable debt for federal income tax purposes. There are certain advantages and disadvantages of issuing pension obligation bonds. The public agency will come out ahead if the retirement system invests the proceeds of the POB and earns more than the cost (debt service and issuance costs) of the POBs and will come out behind if it does not. To learn more about the benefits and risks of issuing pension obligation bonds, please see the resources listed below.

Resources for Pension Obligation Bonds

- California Debt Financing Guide, section 3.3.2.2 Pension Obligation Bonds: https://www.treasurer.ca.gov/cdiac/debtpubs/financing-guide.pdf
- Debt Line, May 2020, "Pension Obligation Financing in California": https://www.treasurer.ca.gov/cdiac/debtpubs/2020/202005.pdf
- CDIAC's presentation, October 24, 2012, "A Double-Edged Sword: The Economics of Pension Obligation Bond Financing for Local Governments": https://www.treasurer.ca.gov/cdiac/webinars/2012/20121024/presentation.pdf
- Government Finance Officers Association advisory, "Pension Obligation Bonds": https://www.gfoa.org/materials/pension-obligation-bonds
- Wulff, Hansen, & Co. "Pension Obligation Bonds: A White Paper": https://www.wulffhansen.com/publications/pension-obligation-bonds-a-white-paper/

4. Lease Revenue Debt – Can you provide more information on lease (revenue) debt?

In lease revenue bond financing, a public agency enters into a lease with a third party (which may be a government, a nonprofit entity, or a for-profit entity). The public agency leases a building or other asset from the third party and the rent paid by the public agency is used to pay debt service on the bonds or certificates issued by that third party and sold to investors. The transactions are structured so that the rent is sufficient to pay debt service and so that the transactions fall within the Lease Exception to the constitutional debt limit.

The California State Public Works Board issues lease revenue bonds for the state, constructs the facility, and leases the facility to the governmental agency user until the bonds are paid in full.

A city, county, or school district that is constrained by the debt limit from issuing general obligation debt may choose to enter into a lease-based financing, such as lease revenue bonds or certificates of participation in order to avoid the time, expense, and political risk of seeking voter approval of the debt; however, lease based financing are paid out of the agency's general revenues and, thus, directly affect operating budgets.

Financing Leases - lease financing is principally used for financing of non-revenue-generating governmental facilities. Lease revenue bonds are a type of revenue bond commonly used to finance state office buildings, facilities, correction facilities, courthouses, and state fire facilities. For more information on lease financing, see resources below.

Installment sale agreements are the preferred financing vehicle for enterprise revenue debt when the issuance of revenue bonds requires voter approval. Installment sale agreement financings are based on a public agency's legal authority to purchase property, including property used by its enterprises and to appropriate annual funds to meet this obligation. For more information on installment sale agreements, see resources below.

Resources

- California Debt Financing Guide, section 3.3.2.1 Lease Revenue Bonds and Certificates of Participation, 3.6.1 Financing Leases, section 3.6.2 Installment Sale Agreements, 3.9.2 State Public Works Board Lease Revenue Bonds: https://www.treasurer.ca.gov/cdiac/debtpubs/financing-guide.pdf
- California State Treasurer's Office publication, 2017, "A Citizen's Guide to State Revenue Bonds": https://www.treasurer.ca.gov/publications/bonds101_revenue.pdf