

# **Bond Case Briefs**

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## **How To Avoid Stepping Into Hazardous Municipal Bond Issues Caused By Covid-19.**

In August I wrote a Forbes column titled, [The Lunacy of Using City Streets To Collateralize New Municipal Bond Deals](#). I received quite a lot of feedback confirming the stupidity of these bonds. I cited two California cities—Torrance and West Covina. Both issued taxable Pension Obligation Bonds (POBs) to plug their unfunded pension liabilities. The bonds were collateralized by the city's streets. I still can't determine how these streets could produce any revenue to make interest payments and maturity redemptions if the city's finances go south.

Fast forward to the present. The city of West Covina, California that issued \$204 million of such bonds recently received an audit report from the state of California pointing out significant "deteriorating financial risks that threatens its fiscal stability." In other words, the city is in financial trouble.

The West Covina bonds were rated A+ by Standard & Poor's just five months ago. What changed? Nothing significant as far as I can tell. The rating was simply inaccurate. It is clear S&P failed in their financial diligence. Also, be aware of who pays the rating agencies for their evaluation—the bond issuers themselves.

Look at the ratings of the bonds you own as they appear on your monthly brokerage statement. Find out when the rating agency last looked at the issuer. Many small- to medium-sized municipal bond deals are rated as of the issue date and never again until the municipality issues new bonds. Don't think that AA rated municipal bond you purchased five years ago still has the same credit metrics to warrant that rating today.

You can chose to look at the issuer's financials yourself. Determine if revenues exceed expenses annually. How much cash do they have on hand? Is it enough to cover any shortfall in revenues until maturity? Find out if the rating agency has recently updated their report on the issuer. These can quickly tell you what has changed and why.

If you are investing in municipal bonds yourself, use EMMA as your go-to source for municipal bond financials.

The large general obligation issuers from fiscally responsible states like Virginia and Maryland or hospital revenue bonds like Cedars-Sinai in Los Angeles and Kaiser Permanente, all have readily available current financials.

If your municipal bonds made it out of the pandemic unscathed, then congratulate yourself. If several of your municipal bond positions were downgraded, you just might want to find out why. Maybe whatever happened is survivable but maybe it's time to get out while you still can.

Stay as far away from hinky deals like Torrance and West Covina as possible. Wrap your arms around your municipal bond holdings—it may save you heartache down the road.

**Forbes**

by Marilyn Cohen

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