Bond Case Briefs

Municipal Finance Law Since 1971

California City That Sold Pension Debt Now at Fiscal Brink.

- **West Covina plumbed reserves to meet costs, state auditor says**
- **City has no recovery plan and risks bankruptcy, audit says**

West Covina, California, which sold $204 million of pension bonds in July, is at the fiscal brink because of its ineffective management and raiding of reserves, according to a report Tuesday by State Auditor Elaine Howle.

The southern Californian city of about 105,000 residents helped cover salary and benefit costs for its public safety workers by siphoning from reserves, halving its year-end balance in fiscal 2019 to about $10 million over four years, the report said.

The city, which has about $227 million in outstanding municipal debt, has made “questionable” financial decisions, has likely understated the impact of the coronavirus pandemic and doesn’t have a fiscal recovery plan, raising the risk of bankruptcy, according to Howle’s report.

“West Covina is at high risk of being unable to meet its future financial obligations and provide effective city services,” the audit said. “If West Covina is unable to resolve its structural deficit, it risks becoming embroiled in the lengthy and complex process of declaring municipal bankruptcy.”

In July, West Covina’s financing authority sold $204 million of taxable lease-revenue debt rated A+ by S&P Global Ratings, with the top yield of 3.89% for a bond maturing in August 2044. A bond due in August 2038 traded Monday at a 3.12% yield, according to data compiled by Bloomberg.

Proceeds of the sale went to paying down the city’s unfunded pension liability, which would initially reduce its annual pension obligation to the California Public Employees’ Retirement System. But that leaves the city on the hook for required debt payments that gradually increase every year by 2044 and still at the risk of higher pension bills should the retirement system underperform its target and require more from municipal governments to make up the difference, the audit said.

West Covina plans to sell land and use the proceeds to pay down its debt obligations, according to the report. But, such “large one-time revenue sources will be insufficient on their own to reverse the city’s negative financial trend and rebuild its reserves,” it said.

City Manager David Carmany said in an interview that he and the finance director were brought in recently to address the city’s fiscal issues. With public safety expenses accounting for about 80% of West Covina’s general fund, Carmany said that officials are negotiating with unions to help defray the burden, and police officers agreed to contribute more toward their pensions. The city may also disband the fire department and instead contract with Los Angeles County for its fire services, a decision that the council may make early next year, he said.

“We are aggressively exploring all options,” Carmany said. “This community is going to be facing some tough choices.”

Bloomberg Markets

By Romy Varghese

December 1, 2020, 11:25 AM PST Updated on December 1, 2020, 2:43 PM PS