

Bond Case Briefs

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Fitch: California State Lease Bond Facilities Not Affected by Wildfires

Fitch Ratings-San Francisco/New York-17 January 2025: Facilities supported by state appropriation-backed bonds remain unaffected by the recent Los Angeles wildfires, according to Fitch Ratings. The California State Public Works Board (SPWB) and the State Treasurer's Office have reviewed the leased facilities in the Los Angeles area for the SPWB bonds and have indicated that none have been damaged by the LA fires.

The SPWB issues appropriation-backed bonds for facilities throughout the state. Each state agency's obligation to pay rent under the various facilities' leases between state agencies and the SPWB is subject to the ongoing use and occupancy of the facility leased under the facility leases. Rent can be abated when there is substantial interference with the use and occupancy of the facility.

Fitch generally rates appropriation-backed bonds one notch below the obligor's Issuer Default Rating (IDR), reflecting the slightly higher degree of optionality associated with lease/appropriation payments compared to the IDR. Fitch believes the incentive and propensity to repay lease/appropriation debt is closely linked to an obligor's incentive and propensity to repay all debt. This reasoning applies to abatement leases and Fitch does not apply additional notching from the IDR when abatement is present. Fitch assumes that the issuer will repay such debt even if it technically has the option not to do so.

This was the case in 2023 when the California Department of Food and Agriculture (CDFA) lost use and occupancy of a bond-financed facility following flooding in Tulare. The obligation of the CDFA to pay rent under the facility lease between the CDFA and SPWB was abated as there was substantial interference with the use and occupancy of the facility. At that time, it was determined that the abated portion was modest relative to the overall lease financing and the SPWB used legally available funds for payment of a portion of one debt service payment. Ultimately, the bonds were defeased through a subsequent refunding issuance and such CDFA facility is no longer subject to a facility lease for any outstanding SPWB bonds.