



Memorandum

TO: PUBLIC SAFETY, FINANCE, AND
STRATEGIC SUPPORT COMMITTEE

FROM: Julia H. Cooper

SUBJECT: SECOND QUARTER FINANCIAL
REPORTS FOR FISCAL YEAR
2020-2021

DATE: February 5, 2021

Approved

Date

2-9-21

RECOMMENDATION

- (1) Accept the Second Quarter (period ended December 31, 2020) Financial Reports for Fiscal Year 2020-2021 for the following programs:
 - (a) Debt Management
 - (b) Investment Management
 - (c) Revenue Management;
- (2) Refer the Second Quarter Financial Reports for Fiscal Year 2020-2021 to the March 9, 2021, City Council Meeting for full adoption.

OUTCOME

Provide the quarterly update on debt management, investment management, and revenue management work efforts.

BACKGROUND

The attached Second Quarter Financial Reports for Fiscal Year 2020-2021 presents the Finance Department quarterly activity for the City Debt Management, Investment Management, and Revenue Management programs (Attachment A). Additionally, the Second Quarter Investment Report has been distributed to the City Council via email and is available on the Finance

Department web page¹. As part of the ongoing effort to streamline work efforts within the Finance Department, these three reports are combined in one single report for submission to the Public Safety, Finance, and Strategic Support Committee ("PSFSS Committee") for its review and acceptance. A brief narrative discussion is provided below for all three components of this quarterly report.

ANALYSIS

This section of the report is divided into the following sections: Debt Management Program, Investment Management Program, and Revenue Management Program.

Debt Management Program

This Second Quarter Debt Report focuses on the City's debt activities for the period ended December 31, 2020, and relates to the following elements of the City's Debt Management Program:

- Completed financings and current debt portfolio
- Debt issuance and management activities completed and anticipated to fiscal year end
- Current interest rate environments and credit ratings

Completed financings and current debt portfolio

- **Completed financings:**

Lease Revenue Bonds:

On October 15, 2020, the City of San José Financing Authority (CSJFA) issued Taxable Lease Revenue Bonds, Series 2020B in the amount of \$146.5 million for the Ice Centre Expansion Project. The 2020B Bonds also refunded all of the Series 2008E Bonds, issued for previous Ice Centre expansion projects.

Multi-Family Housing Revenue Bonds:

Page Street Apartments - In November 2020, the City served as a conduit issuer for \$29.5 million in tax-exempt 501(c)(3) revenue bonds for Page Street Apartments to finance the acquisition, construction and development by Charities Housing Development Corporation (a California nonprofit corporation) for an 82-unit affordable housing project for low/very low-income residents in San José.

¹ <https://www.sanjoseca.gov/your-government/departments/finance/reports/-folder-450>

Alum Rock Apartments - In November 2020, the City served as a conduit issuer for \$36.9 million in tax-exempt 501(c)(3) revenue bonds for Alum Rock Apartments to finance the construction and development by Affirmed Housing Group (a California for-profit corporation) for an 87-unit affordable housing project for low/very low-income residents in San José.

- **Current Debt Portfolio**

The City's total outstanding debt portfolio as of December 31, 2020 is \$4.8 billion, of that amount, \$3.9 billion is direct debt issued by agencies of the City and \$828 million is conduit debt for multifamily housing. The amount of debt issued (agency and conduit) for the first two quarters of FY 2020-21 is \$712.2 million.

Debt issuance and management activities completed and anticipated to fiscal year end

- **Debt Issuance**

Pre-issuance activities – the City is currently engaged in pre-issuance activities for Airport Refunding Revenue Bonds, scheduled for Council approval on March 9, 2021 for potential bond sale in late March 2021 and bond closing in early April 2021. The City also is planning for Retirement System Prefunding scheduled to receive Council consideration in June and issuance in July, and General Obligation Bonds and Lease Revenue Bonds tentatively scheduled for Council approval and issuance in the first quarter of Fiscal 2022.

- **Debt Management**

Requests for Proposals (RFP) - In December 2020, the City released an RFP to Municipal Advisory Firms to advise the City on options for funding its annual obligations to fund retirement system payments including the unfunded actuarial liabilities of the two retirement systems. The RFP was split into two (2) phases of engagement to provide advice on (1) funding options and (2) advice during the bond issuance process if Council elects to issue pension obligation bonds following its study session, tentatively scheduled for April 23, 2021.

Reporting – During this period, debt management staff completed and submitted the required CDIAC Mello-Roos Annual report (October 2020), submitted the Annual Continuing Disclosure (Community Facility/Improvement Districts) as required by the MSRB, and issued the 2020 Comprehensive Annual Debt Report (CADR).

Current interest rate environments and credit ratings

- **Current interest rate environment**

Fixed Rates – over the last 10 years, the historic tax-exempt long-term (20-year maturity) interest rates averaged 3.34%, it's currently at 1.74% (as of 1/21/21).

Variable Taxable and Tax-Exempt Interest Rates - Tax-Exempt SIFMA weekly interest rates averaged 0.11% in Q2 and are currently at 0.05% (as of 1/20/2021). Taxable LIBOR monthly interest rates averaged 0.15% in Q2 and are currently at 0.13% (as of 1/21/2021).

LIBOR Update –The London Interbank Offered Rate (LIBOR) has been used in the calculation of interest and other payments in banking and finance, commonly used by the City (1-month and 3-month LIBOR) for its Commercial Paper interest cost calculation, for budgeting purposes and certain bank agreements. Because of the financial crisis of 2008 and the LIBOR manipulation by several financial institutions in 2012, regulators grew wary of overreliance on that particular benchmark and established a scheduled phased out in December 2021 substituting with an alternative reference rate, SOFR (Secured Overnight Financing Rate). On November 30, 2020, the Federal Reserve announced that LIBOR will be phased out and eventually replaced by June 2023; banks were instructed to stop writing contracts using LIBOR by the end of 2021 and all contracts using LIBOR should wrap up by June 30, 2023.

- **Credit ratings**

The City's current general obligation bonds are rated Aa1/AA+/AA+ and lease revenue bonds are rated Aa2-Aa3²/AA/AA and AA-, by Moody's Investors Services Inc. ("Moody's"), Standard & Poor's Ratings Services ("S&P"), and Fitch Ratings ("Fitch"), respectively. All three rating agencies also affirmed the City's General Obligation (GO) rating of Aa1/AA+/AA+ in conjunction with assigning their new ratings for the lease revenue bond issuances in September 2020 (Civic Center Refunding, Series 2020A) and October 2020 (Ice Centre Expansion, Series 2020B). All three rating agencies have maintained their respective Sector Outlook as Stable for GO and lease revenue bonds.

On October 1, 2020, S&P downgraded the City's outstanding Airport Revenue Bonds to A- (from A), Negative Outlook. On October 22, 2020, Moody's affirmed the City's outstanding Airport Revenue Bond rating of A2 during its periodic review process. The rating agencies continue their Negative Outlook for the transportation and airport sectors as a result of the economic impacts of the COVID-19 pandemic. In January 2021, S&P updated their U.S. Transportation sector credits (including Airports) stating that the airport sector faces a long

² Moody's and Fitch determine its lease revenue bond ratings in part based on "essentiality" of leased asset; bonds tied to an essential asset, like City Hall carries higher rating (Aa2) than bonds tied to a less essential asset such as Convention Center (Aa3) and Ice Centre (AA-).

recovery relative to other transportation subsectors; annualized declines of approximately 40% for airports recovering to approximately 15% below pre-COVID-19 levels by the end of 2023. Outlooks on individual debt ratings on airport-related issuers sensitive to changes in ridership and air travel demand, are likely to remain negative. Outlooks indicate rating agencies' view regarding the potential for a rating change and the direction of the change, so a negative outlook indicates a rating may be lowered. The timeframe for an outlook is generally two years, but the City expects to make presentations to the rating agencies regarding the Airport credit in March 2021 in conjunction with the proposed refunding of the Airport's Revenue Bonds for economic savings and short-term budget relief due to the pandemic.

Investment Management Program

A quarterly investment report for the period ended December 31, 2020 is posted on the Finance Department website. Pursuant to the City's Investment Policy, verbal presentations in addition to the written reports are provided to the PSFSS Committee for the Second and Fourth Quarter Reports. The materials presented in this consolidated report provide a "snapshot" of the investment portfolio. The report will be agendaized for acceptance by the City Council pursuant to the Investment Policy.

Revenue Management Program

The Revenue Management report highlights the key aspects of the City's ongoing collection efforts. These efforts focus on reducing delinquent accounts receivable and enhancing revenue compliance through four (4) primary collection programs: Accounts Receivable, Business Tax, Revenue Compliance and Monitoring, and Utility Billing. This report provides the highlights of the Revenue Management Division's collection efforts and summarizes the progress towards maintaining a return on investment ratio of 5.5 to 1. Actual year-to-date return on investment through the second quarter of fiscal year 2020-21 is 5.9 to 1. This report also includes a status summary of the Business Tax Amnesty Program ("Amnesty Program").

Business Tax COVID-19 Assistance

The City of San José is offering a temporary expansion of business tax financial hardship exemptions. The expansion increases eligibility for existing financial hardship exemptions to any business, in addition to small business owners, that meet the income requirements. The income requirements are as follows:

- Businesses with gross receipts of \$25,520 or less in the 2020 calendar tax year are eligible for the financial hardship exemption for low revenue generating businesses.
- Business owners with adjusted gross income of \$51,040 or less in the 2020 calendar tax year are eligible for the financial hardship exemption for business owners with limited household incomes.

Additionally, the Finance Department will allow businesses to apply for a financial hardship exemption based on their anticipated 2020 income, rather than relying on income reported on 2019 tax returns. The expansion is in effect from October 1, 2020 through September 30, 2021.

Businesses and residential landlords with renewals due this quarter were notified about the expanded COVID-19 assistance and nearly 350 have applied for the exemption.

CONCLUSION

The Financial Reports provide information and transparency of the Finance Departments debt, investment, and revenue management activities for the quarter.

EVALUATION AND FOLLOW-UP

The Finance Department prepares this report on a quarterly basis for review and approval by the PSFSS Committee. The Finance Department staff will be available to answer questions on the Second Quarter Financial Reports for Fiscal Year 2020-2021 at the PSFSS Committee meeting on February 18, 2021 and the City Council Meeting on March 9, 2021.

CLIMATE SMART SAN JOSE

The recommendation in this memo has no effect on Climate Smart San José energy, water, or mobility goals.

PUBLIC OUTREACH/INTEREST

This memorandum will be posted on the City's website for the February 18, 2021 PSFSS Committee meeting and the March 9, 2021, City Council meeting.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office and City Manager's Budget Office.

COMMISSION RECOMMENDATION/INPUT

No commission recommendation or input is associated with this action.

/s/
JULIA H. COOPER
Director of Finance

For Debt and Treasury Management questions, please contact Nikolai J. Sklaroff, Deputy Director at (408) 535-7832 and for Revenue Management questions, please contact Rick Bruneau, Deputy Director at (408) 535-8310.

Attachment A: Second Quarter (period ending December 31, 2020) Financial Reports Presentation for Fiscal Year 2020-2021