



## City of Port Huron, Michigan

**\$52,710,000 of General Obligation Limited Tax Pension Bonds, Series 2020 (the "Bonds" or "POBs")**  
**"A+" S&P Ratings**

**March 2020**  
**Sole Manager**

### Use of Proceeds/Security:

- The bonds were issued to pay a portion of the City's UAAL in its retirement program.
- The bonds were secured by the City's limited tax, full faith and credit pledge.

**Port Huron's Retirement Program:** The City's retirement program is an agent multiple employer defined benefits pension plan administered by the Municipal Employees' Retirement System of Michigan ("MERS").

- Included 660+ members and was funded to 55% and had a UAAL of approximately \$70 million at year-end 2019.
- The City is required by MERS to make annual contributions to its pension plan ("ARC"). The ARC is the actuarially determined amount necessary to fund the benefits earned by employees during the year (i.e. the normal costs) and the amount needed to amortize the UAAL. The City experienced increasing payments on its ARC that caused budgetary strain.
- At the onset of 2020, the City changed its actuarial rate of return assumption from 7.75% to 7.35% and its wage inflation assumption of 3.75% to 3.00% which increased the UAAL to \$78 million.

### Structuring the Pension Bonds:

- In our hypothetical analysis and interest rates at that time, Baird illustrated potential savings the City would generate if they issued the Bonds as taxable in the public market and use the bond proceeds to retire a portion of its UAAL versus how the City currently funded its UAAL.
- While our initial analysis illustrated the potential for savings, it was paramount to Baird that the City understand and become comfortable with the risks. Through multiple conversations with the City Manager, Baird clearly communicated the importance of the City's evaluation of the risks associated with issuing POBs including the negative press associated with the POB approach.
- Due to the budgetary strain of its increasing ARC payments and with extensive negotiations, the City and Baird were able to get MERS to grant a one-time extension of the amortization of the City's UAAL to 2049 predicated on, among other things, the City's ability to partially fund its UAAL with the bond's proceeds with equal distribution between the various funds of its pension plan.

### Rating Agency Approach:

- The rating agencies claim that they are neutral on the use of POBs. Baird has found that that is true only when the client has a well-thought-out approach and strategy that demonstrates that management has considered the risks of POBs and has a concrete plan in mitigating the perceived risks.
- With Baird's assistance, the City's rating was affirmed at "A+" by S&P. S&P writes in its January 28<sup>th</sup> report: "We do not view pension liabilities as an immediate source of credit pressure for Port Huron given the POBs will refinance a large portion of the city's pension liability into a fixed-debt obligation..."

**Pricing:** As the City's Bonds were preparing to price, the dark clouds of the pandemic were on the horizon.

- Baird recommended that the City enter the market as soon as possible to avoid a negative, severe market reaction to the increasingly negative market tones.
- The bonds were priced on March 3<sup>rd</sup>, a week prior to the market's dislocation as the pandemic shutdown the economy and State. The City achieved a bond rate of 2.84%, well below the 7.35% it was paying to MERS.
- Assuming MERS achieves 7.35%, the City will achieve expected gross savings of \$87.4 million. The present value of that amount is \$52.6 million (99% of the UAAL funded).

## **Baird Public Finance**

### **Warren Creamer**

Managing Director

231-933-8447

[wcream@rwbaird.com](mailto:wcream@rwbaird.com)

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