MINUTES

SOUTH BAYSIDE WASTE MANAGEMENT AUTHORITY
MEETING OF THE FINANCE COMMITTEE
Tuesday, January 10, 2023 12:00PM
Via Zoom Tele or Video Conference

Call To Order: 12:04PM

1. Roll Call

Member	Present	Absent
Michael Brownrigg		X
Rebecca Mendenhall	X	
Rich Lee		X
Al Royse	X	
Jay Benton	X	

SBWMA Staff Members Present: Joe La Mariana, John Mangini, Joanne Nghiem, Cyndi Urman, Jean Savaree,
Others Present: John O'Neill, Jared Beck, Drew Public Attendee

2. Public Comment

Pursuant to Government Code Section 54954.3(a), members of the public wishing to address the Committee may do so, and the comments shall be limited to the Special Meeting notice topic(s). Speakers may join the Zoom meeting via the meeting link and using the "raise hand" feature and the Clerk of the Board will call on people.

None

3. Executive Director's Welcome *(Verbal Only)*

Executive Director La Mariana welcomed everyone to the meeting and gave the following updates.

There was serious flooding over the weekend at Shoreway. The loading tunnel is the low point on the property, it has flooded in the past, but on New Year's Eve there was 20 feet of water in the tunnel. He thanked the City of Belmont for loaning the agency a high-powered pump, to remove the water from the tunnels and get the facility back up and running by January.
He noted that this storm has highlighted the vulnerability of the site, and he wanted to have a discussion with the City of Belmont and San Carlos to talk about the flooding and discuss resurfacing the road.
Staff is completing the first phase of any future master plan, which is the site optimization study. The high concept drafts will be discussed at the January Board meeting. Should the board see the value in modifying the site, this committee would need to talk in conceptual terms about financing options, and eventually go back to the Board with plans for a Master Plan process. The process would likely mean an additional Finance

Committee meeting this spring.
Board Member Brownrigg has expressed interest in adding a third elected official to the Finance Committee, so there will be an item on the January Board agenda to add an additional Finance Committee member from the Board of Directors.

Member Benton commented that his role was meant to have been an interim role on this committee, and he was ready to step off the committee.

Member Royce asked if there were abnormal costs that needed to be picked up because of the flooding.

Executive Director La Mariana noted that the Recology administrative building did sustain damage on the first floor. Reconstruction costs are additional costs outside the budget that will be incurred, but the costs are currently unknown, and this committee and the board will have a conversation regarding emergency funding once the full scope of the repairs are complete.

Member Mendenhall commented that staff should take care to take pictures of the damage and record all of the repair costs. Right now the City of San Carlos is in the data gathering stage which will then go to the County to get consolidated information across agencies to submit to CalOES which will then go FEMA. The amount of funding is unknown at this time, but information should be out in the next few weeks.

4. Consent Calendar

Consent Calendar item(s) are considered to be routine and will be enacted by one motion. There will be no separate discussion on these items unless members of the Committee, staff or public request specific items be removed for separate action. *Items removed from the Consent Calendar will be moved to the end of the agenda for separate discussion*.

A. Approval of the Minutes from the October 18, 2022, Finance Committee Meeting

Motion/Second: Royse/Benton
Roll Call Vote: 3-0-0-2

Member	**Yes**	**No**	**Abstain**	**Absent**
Michael Brownrigg				**X**
Al Royse	**X**			
Jay Benton	**X**			
Rebecca Mendenhall	**X**			
Rich Lee				**X**

5. Draft for Finance Committee Review: Resolution Approving the SBWMA Investment Policy for 2023

Staff Mangini gave an overview of the staff report and highlighted the changes recommended for the 2023 edits.

Member Mendenhall asked that the government code for reporting time of 30 days versus 45 days in policy be confirmed. Her understanding was the government code still says 30.

Staff Mangini noted that there was a senate bill that passed in September and according to PFM as of January 1, 2023 it is 45 days, but he would double check it.
Member Benton asked if Local Government Investment Funds listed in paragraph 9 are different from Local Agency Investment Funds that the Agency has been investing in for many years.

Staff Mangini answered that this would be an additional option which may have higher yielding returns.

Motion/Second: Benton/Mendenhall (once verified on the government code reporting time)
Roll Call Vote: 3-0-0-2

Member	Yes	No	Abstain	Absent
Michael Brownrigg				X
Al Royse	X			
Jay Benton	X			
Rebecca Mendenhall	X			
Rich Lee				X

6. Green Bond Status Report and Finance Committee Input on Potential Green Bond Eligible Projects

Staff Mangini noted that this item is a report out for the group and gave an overview of the staff report and explained the 2 tables in the staff report.

Executive Director La Mariana noted that with the change in operating contractor in 2024, staff would like the new contractor to have input into the design and implementation of MRF Phase II upgrades. Staff anticipates those costs being between $6-8M, and the funds for those upgrades would come from a portion of these remaining bond funds.

This item was a report out for the committee on the status and there was no further discussion.

7. Follow up from September SBWMA Board Meeting Action Item: Finance Committee Investment Fund Discussion

Staff Mangini noted that this is at the request of Member Brownrigg for the Finance Committee to discuss expanding the list of eligible investments and changing the criteria to allow more flexibility in interest rates to yield higher returns.

Member Benton asked if September and December investments had any substantial differences than the June report included in the packet. He noted that the Lehman collapse has caused a cloud that's been hanging over the County Pool for many years.

Staff Mangini noted he would look up the September and December numbers and see if there was significant change.

Member Mendenhall commented that the primary purpose of this investment fund has always been the safety principle. When the Lehman Brothers fiasco happened, money was moved away from the County, because the County was a little more aggressive than LAIF. The Board and this finance committee can make a decision to become more aggressive in investing, but her opinion was that the safety of public funds was more important than chasing returns.
Member Benton didn't disagree, but with the County having a slightly higher return than LAIF at the moment, he thought it was worth discussing.

Staff Mangini noted that the return for both the County Pool and LAIF had been going back and forth as to which one was giving a better return.

The Committee gave direction to staff to take no action at this time.

8. Review of Agency Specific Financial Models and Recommendation for Creating a Captive Insurance Plan

Staff Mangini gave a brief overview of the staff report and noted that staff continues to look into creating a captive insurance plan to counter the rising costs of insurance premiums. He introduced John O'Neill and Jared Beck from the Agency's insurance broker's Risk Strategies.

John O'Neill noting that formulating a Captive is a long-term vision to make sure there is availability of insurance going forward and not being reliant on fickle markets. He added in this particular industry it's becoming more and more difficult to build the appropriate layers of coverage and predict and stabilize costs.

Staff Mangini added that this committee discussed creating a Captive at a past meeting and had asked Jared to come back with pro forma modeling, so this presentation will focus on Agency specific models.

Jared Beck gave a presentation reminding the committee of Captive Insurance basics as well as 5-year pro forma modeling. In addition, the presentation included extending that 5- year modeling to project out from not just building insurance as an asset, but also when the Agency would see relief on the premiums.

Member Royse asked for a basic refresher from the last discussion, noting that there is a period of time where the Agency is taking on more risk until the fund is built up and the risk becomes more manageable. He asked where the breaking point is.

Jared Beck answered yes, The Agency would front the captive in the first years, so if there was a full limit loss in the first years of creating the captive the Agency would have to eat that, but if the Agency has had five years of success and built up a surplus over time, then loss is a lot easier to absorb. He pointed out that in their 10-year pro forma example the Agency can get to a point where you decide not to invest in the reinsurance because a loss isn't as much of a shock to the system.

Member Royse noted that the example looked like 3-4 years of high risk, and at that point investing the Captive would likely pay off.

Jared Beck answered that the risk never goes away, you would be building an insurance asset and slowly over time taking on additional risk.

Member Benton asked for clarification, in 2022 the insurance premium was $2.1M with a $1.5M deductible. With the captive creation the premium would be $856K. So would this reduce operating expense by the difference between $2.1M and $856K.

Jared answered not necessarily because this scenario just looks funding for the $1.5M deductible, using the Captive to provide insurance for the deductible. So that doesn't reduce the costs per se, that just formalizes the funding of the deductible from the self-insurance fund.

Staff Mangini added further clarification. In this scenario the Agency would be able to reduce the $2.1M premium by the reinsurance program fee. We would be moving money from our reserves account into the Captive account to build an insurance asset over time. In this scenario the Agency would save a couple $100K a year by taking on an additional $1M in risk in the excess layer in addition to the deductible, and managing risk. If that happens for a few years in a row without significant claims, then the asset gets built over time by funding that top line deductible reimbursement. This Captive will either get funded out of reserves or come out of Agency profitability.

Member Benton asked Jared to explain the risks if there was a catastrophic event in years one or two of creating the captive.

Jared Beck answered that the insurance coverage would stay the same, and the Captive would pay the losses instead of the reserves or self-insurance funds. The excess policy would stay the same, but now when the excess premium is paid, and there are no losses the premium stays with the carrier. He thought the rates to the rate payers would be level in the early years of the Captive because you still need to pay the premiums, if the Agency keeps collecting the excess coverage in the early years, then in 5 to 10 years those savings will materialize, and be passed back to the rate payers.

Member Benton asked what kind of reinsurance the agency would have when the $5M excess layer is retired.

Jared Beck answered that after 5 years the Agency would graduate from the 80/20 model and would gain reinsurance for 50% of the excess.

Member Benton asked how much purchased insurance we do have today. And under the Captive at year 5, would there still be $65 worth of purchased insurance.

Jared answered $65M in just property insurance and business interruption, and yes with the captive there would still be $65M in coverage, but in addition to the $1.5M deductible there would be $2.5M into the excess. So, at that point there would be $3.5M in primary retention, and $65M in total limits.

Member Benton asked if there has been a year that we've had a loss over the deductible other than 2016.

John Mangini answered no.

Member Mendenhall wondered how realistic this 2% loss ratio is, she thought that was pretty low, and incidents were more than $17,000 per year. She recommended changing the model to increase those loss ratios because the Agency will still have to insurance premiums of $2.2M, it's just that the surplus would fund an alternative method to fund deductibles.

John O'Neill agreed and commented that the Captives are really for best in class clients, and despite the two fires in 2016, the Agency runs a tight ship and has invested heavily in loss control. And if the Agency continues to invest in loss control you should see better loss outcomes. But if the insurance markets are not giving you breaks based on the investments you are making, he thought long term a Captive made sense.

Member Royce commented that he didn't think there was really any choice. If we do nothing then we're governed by the markets. This allows the agency to take control and try to minimize costs. That being said he thought this had the potential to be an additional cost in the first 3 to 5 years. If we have no losses in that 3-5 year period then there is built up equity that gives a longer term benefit.

Executive Director La Mariana noted that not only has the loss history affected premiums, but the insurance industry has had a lot of catastrophic events, like floods and wildfires that have affected premiums. Does that play into this discussion, and will a Captive give the Agency more control and shielding from those sorts of events.

Jared Beck and John O'Neil agreed and noted that the property insurance is in a state of shock right now and suggested that all the investments the Agency has made in safety could potentially mean that the Agency is subsidizing other properties that are tougher risk.

Staff Mangini summarized that based on the model in the presentation the agency would be funding $2.5M to start a Captive, and then each year the top line deductible reimbursement premium will come from the Agency. He asked if the $655K comes out of the $2.5M or if it is additional funding for each subsequent year.

Jared Beck answered yes, you would fund both each year. This model illustrates the agency funding premium to cover the $1.5M retention. There is somewhat of a savings on the premium and the Agency would take that savings and put it into the Captive.

Staff Mangini commented that if the Finance Committee chooses this kind of funding model that would be the outflow of money for the Agency, so he wanted to make sure that was clear.

Member Royse asked if the $655K would be funded from reserves, and if so, what was the current reserve balance.

Staff Mangini noted that the reserve is currently right about $5.8M, and if not taking out of reserves the only other option is through rate increases. He did note that the emergency reserve is there for catastrophic events that aren't covered by the current property insurance policy, so this would obviously expand the risk, but the reserve is specifically for this, so maybe moving to a captive over time makes sense, but it would reduce the emergency reserve and the self-insurance reserve. It would be moving the money from one controlled asset to another controlled asset and using the money specifically for insurance claim incidents. The other impact would return on investment from the investment portfolio, because reserve balances are in the investment portfolio.

Member Benton asked what the $2.5M would do to the overall reserves.

Staff Mangini answered the self-insurance fund and the emergency reserve fund together are about $6.4M.

Member Mendenhall commented that she thought the emergency reserve needed to be kept at a certain percentage of expenses.

Staff Mangini answered that the emergency reserve is up to 10% of the expenses of the budget, he didn't know if the Captive could be considered as part of the reserves.

Member Mendenhall asked if the Agency took the money from the two reserves to fund the captive would that cause the emergency reserve to go below the 10%.

Staff Mangini noted that the policy is up to 10%, so there isn't a 10% threshold. It's currently at 9%.

Rebecca wanted to make sure the Board understood what the percentage would go down to if they decided to fund the Captive, because they would have adopted a certain percentage when they adopted the budget. She added that she would be more comfortable creating a Captive out of the reserves, but it needs to be made clear to the Board. The other option is to look at what the Captive would like if not funded as high as this model, it would take a lot longer to get to the numbers the Agency is trying to get to, but it would become its own entity over time and more money could be put in at any time.

Member Royse agreed but noted that he was concerned that the insurance rates would go up faster than the rate of funding the captive and the sooner we can manage risk the better, but it will take the reserve balance down 3 to 3.5%.

Member Benton thought more conservative loss assumptions were needed, because if something bad happens the board is going to have to explain to the rate payers their insurance decisions, and even if it slows the captive down, the priority has to be protecting the rate payers.

Executive Director La Mariana asked the Committee if they were comfortable with proceeding with a recommendation to the Board to move forward with approval of the work plan to create a Captive.

Member Benton commented that he would like to see an alternative model to the assumptions presented today, that would represent a worst case scenario that would demonstrate creating a Captive wouldn't crater the whole agency.

Member Royse added in addition to looking at all of the adverse scenarios he'd like to see a presentation of pros and cons that clarify the additional risks and costs that the Agency will absorb by creating a Captive. The benefits and risks need to be made clear.

Member Mendenhall reiterated also included the impacts to reserves based on the dollar amount of the funding be included in the report to the Board.

Member Benton that fundamentally what the board needs to understand. One, what is the impact to the rate payers while the Captive is getting fully funded. And two, what risk is being added by insuring this way. And he thought the presentation to the full board needed to be simplified.

9. Discussion and Recommendation of 2023 Finance Committee Meeting Calendar

The Committee discussed Member Mendenhall's request to move the time of the meeting to 1PM.

The committee will meet at 1PM going forward.

10. Finance Committee Member Comments

11. Adjourn 2:08PM