EL DORADO LAFCO

LOCAL AGENCY FORMATION COMMISSION

AGENDA OF MAY 27, 2009

REGULAR MEETING

TO:	**Francesca Loftis, Chair, and** **Members of the El Dorado County Local Agency Formation Commission**
FROM:	**José C. Henríquez, Executive Officer**
AGENDA ITEM #4:	**CONTINUED PUBLIC HEARING TO CONSIDER AND ADOPT THE FINAL BUDGET FOR FISCAL YEAR 2009-10**

RECOMMENDATION

Staff recommends that the Commission:

1. Receive the information related to the General Liability Insurance allocation;
2. Receive the information related to the adopted Proposed Budget for Fiscal Year 2009-2010;
3. Open the Public Hearing on this matter;
4. Approve the Final Budget for 2009-2010 by adopting Resolution L-2009-05; and,
5. Direct staff to transmit the Final Budget to the funding agencies and others as specified in Government Code §56381.

REASON FOR RECOMMENDED ACTION

El Dorado LAFCO adopts its own budget with notice to all funding agencies. The approved Proposed LAFCO Budget provides adequate funding for the El Dorado LAFCO to meet the responsibilities of the Cortese-Knox-Hertzberg Act; however the Commission did not approve a final budget at the April meeting because of questions related to the general liability insurance for Fiscal Year 2009-2010.

BACKGROUND

This report will be divided into three sections, reflecting the direction that the Commission provided to staff at the April meeting. The first section relates to the question of whether LAFCO is prohibited under State Law to create reserve funds in its budget. The second section relates to general liability insurance with a recommendation by the Budget Ad Hoc Committee on how to proceed. The third section relates to the budget overall.

Reserves

The question of whether LAFCOs are allowed under the law to establish reserves was raised during a discussion of the Commission establishing a legal defense fund. The LAFCO budget is governed by Government Code §§56381 and 56381.6. These sections address the timelines for adoption and the transmittal of the LAFCO budget [GC §56381(a)]; the apportionment methodology to be used by the County Auditor [GC §56381(b)] and an alternate methodology for LAFCOs with different representation (GC §56381.6); and the requirements for payment by the funding agencies [GC §56381(c)]. The only limit to the Commission's authority on setting its own budget relates to ensuring the adequate funding for this agency. The second paragraph in GC §56381(a) reads:

> At a minimum, the proposed and final budget shall be equal to the budget adopted for the previous fiscal year unless the commission finds that reduced staffing or program costs will nevertheless allow the commission to fulfill the purposes and programs of this chapter.

According to various sources, the impetus for this sentence was to prevent funding agencies from "choking" a LAFCO by withholding funds. In the past, several home counties rendered their LAFCOs irrelevant by underfunding them. Without adequate revenues, those LAFCOs could not hire staff or otherwise meet their obligations or mandate. Consequently, the Legislature inserted this language into the Cortese-Knox-Hertzberg Act (CKH) to prevent such punitive measures.

Since no other sections of CKH concern LAFCO's budget, there is no statutory restriction on establishing reserves for legal expenses or some other restrictive purpose. Establishing reserves are helpful for:

- Minimizing the impact of a significant drop in revenue
- Minimizing the "rate shock" to the funding agencies in case of significant budgetary increases
- Planning for future known expenses (such as outsourcing studies)

For purposes of providing context, currently there are sixteen LAFCOs that have reserves for legal defense, professional services or both. Two additional LAFCOs have reserve accounts for other purposes (retiree health benefits).

General Liability Insurance

As discussed in previous months, the County of El Dorado notified LAFCO that the general liability insurance (GLI) premium for the current fiscal year and next fiscal year will be approximately $30,000 each. In January the Commission took steps to cover this increase for Fiscal Year 2008-09 and directed the Budget Ad Hoc Committee and staff to research new general liability insurance carriers and return with a recommendation. In March, the Commission elected to participate in the SDRMA program and adopted Resolution L-2009-03 to start the process. In April, as a result of a letter submitted by County Risk Management, the Executive Officer learned that the SDRMA program does not cover the legal costs in the scenario with the biggest exposure to this agency. The scenario, typically called “injunctive relief” or “declaratory relief” lawsuit, is the situation where a party sues LAFCO to set aside a LAFCO decision or determination. Typically, injunctive relief cases do not involve damage claims.

In addition to researching whether LAFCO can have a legal reserve, the Commission directed the Budget Ad Hoc Committee and staff to do the following:

1. Request that County Risk Management compare its program with SDRMA’s program to identify the areas, if any, where coverage is not the same; specifically, whether personal liability protection is included in the SDRMA program.
2. Verify whether Alliant Insurance’s program covers injunctive/declaratory relief coverage.
3. Research whether SDRMA or another carrier would be willing to underwrite or sponsor separate cover for injunctive relief to cover the legal defense costs.
4. Verify whether SDRMA’s coverage is occurrence based and whether there is a policy limit.

Insurance Coverage

On May 6, 2009, Larry Costello from County Risk Management provided LAFCO staff with both a summary and a detailed analysis comparing the County GLI coverage to the SDRMA program. Overall, the SDRMA program is comparable to the current insurance obtained through the County. A synopsis from Mr. Costello is attached to this memo as Attachment A. The more detailed report is not included because of its size; however, it is on file at the LAFCO office and it can be provided electronically to any Commissioner who wishes to see it. Please note that of the items of interest, Commissioners’ “personal liability protection” and “errors and omissions” coverage, the programs are similar. Please note the following:

- Mr. Costello indicates in his synopsis that the SDRMA program does not exclude coverage for injunctive/declaratory relief lawsuits; however, I verified with SDRMA and have found the specific location of the exclusion in the Terms and Conditions.
- Because the County’s coverage is self-funded up to $1 million, it covers the defense costs in injunctive/declaratory relief cases. However, the California State Association of Counties (CSAC), which the County uses to buy excess insurance, does not cover those expenses. Effectively, this means that should the Commission retain the County coverage, its limit would effectively be $1M, not the $15M limit that is the coverage for other aspects of the County’s program.

SDRMA and CSAC voluntarily compared their own programs against one other. They verified Mr. Costello’s findings that the coverages for most of the items are the same. A letter from SDRMA reporting their analysis is included as Attachment B to this report.

Injunctive/Declaratory Relief Coverage

As noted above, the Commission requested that staff pursue whether separate coverage for injunctive/declaratory relief protection can be purchased. In addition, it directed staff to determine whether the Alliant program had such a coverage built into its plan.

At the time of this writing, staff was not able to verify whether the Alliant Insurance program, as quoted to staff in February, covered injunctive/declaratory relief. However, Alliant agreed to re-circulate an underwriting request among its partners to provide just that coverage. A similar request was made to SDRMA, AON Worldwide and ISU Insurance Services - Atwood Agency, the latter two being commercial insurance brokers.

SDRMA and Atwood were unable to find any partners willing to underwrite that coverage. Staff will forward any new information from AON Worldwide or Alliant regarding supplemental coverage should it receive it after the packet has been mailed out on Monday, May 17.

Lastly, staff verified with SDRMA that their policy limit is $1.5 million per occurrence.

Recommendation

The Commission is in a difficult situation with GLI. As the Budget Ad Hoc Committee and staff see it, the options before the Commission are the following:

1) Retain the County as the insurance carrier. The Commission will have to raise agency contributions by at least $30,000. The Commission will have to rescind Resolution L-2009-03 if it chooses this option;

2) Continue with February's plan to participate in the SDRMA program but start budgeting a reserve to cover any potential legal defense costs;

3) Although we have no documented proof, contract with Alliant in the hope that injunctive/declaratory relief is covered. The Commission would have to start a reserve anyway because the deductible under the Alliant plan is $10,000. The Commission will have to rescind Resolution L-2009-03 if it chooses this option; or

4) Continue with February's plan to participate in the SDRMA program, not establish a reserve and hope for the best.

The Budget Ad Hoc and staff recommend Option #2 for the following reasons. First, all but the fourth option involves having to increase the agency contributions, so there are no true cost savings in any scenario. Second, Option #4 leaves the Commission in a position that, given the discussion at the April 22nd Meeting, it was not comfortable with. Third, Option #3 is not a viable alternative because there is no written guarantee that injunctive/declaratory relief is covered in the Alliant program.

As discussed in the January and February meetings, this agency has experienced fluctuating GLI premiums in the past seven years with the County. While the coverage is extensive, it has also proven to be expensive and unpredictable for staff to budget. Next year's premium is estimated to be between $30,000-35,000, which is almost 7% of the budget. The cost allocation formula that the County uses to set its premium has changed twice in the past four years, affecting the agency's premium significantly. For staff to recommend this option would be difficult given the Commission's desire for fiscal prudence; especially when considering that $30,000-35,000 is being used to purchase insurance for an agency of 11 Commissioners, 3.5 staff (at full capacity) and a budget of less than $500,000. Finally, LAFCO has no memorandum of understanding with the County on GLI. That means LAFCO has no procedure to request the lowering or negotiating of its premium; nor is the County bound to honor those requests.

There is the option for the Commission to negotiate an MOU with the County. It can elect to appoint the Executive Officer or an ad hoc committee to meet with the CAO and County Risk Management to do this on its behalf. A risk management consulting firm can also be contracted to negotiate on LAFCO's behalf. Bringing in a consultant would entail them obtaining and reviewing the County's claim cost allocation formula and their calculations to ensure that they are correct. Depending on what is found, the consultant could also examine LAFCO's loss history and current risk exposure to calculate the potential for loss. However, there is a significant amount of uncertainty with this approach. First, the County has not been open to offering an MOU in the past. Second, the County has also not been responsive towards negotiating a lower premium. Third, there is also the possibility the County may not want LAFCO to participate in its risk pool any more. If the latter is true, the Commission may miss the window to participate in the SDRMA program since they only cover members on a fiscal year basis. If the negotiations with the County are unsuccessful, then the Commission may find itself without coverage for FY 2009-10.

Option #2 provides an opportunity to purchase a more cost effective policy that is just as comprehensive. Currently, LAFCO contracts with SDRMA for Worker's Compensation Insurance and the rates have remained stable for the past five years. There is every reason to believe the same will hold true for GLI. In addition, establishing a reserve would be a prudent measure that would give the Commission a peace of mind in case it would ever need it. The reserves provide the Commission with the flexibility to use those funds for other purposes besides covering legal costs for defense. For example, it gives the Commission the ability to plan for other future expenses, such as funding for studies or any other large outlays. The Commission could also structure the reserve so that it specifies the timing or manner in which it will use those funds or determine that it would take a supermajority of Commissioners to approve the use of the funds. Either or both of those measures would ensure the proper use of those monies.

Staff would recommend allocating $20,000 a year into a reserve up to a limit determined by the Commission to be acceptable. Given that the last two lawsuits against LAFCO were less than $100,000, staff would recommend a reserve limit of approximately this amount. While it means that the agency contributions will have to be increased, it will be a short-term proposition until the reserve limit is reached. The Commission may direct staff to return with proposed language at the June or July meeting to incorporate into its Policies and Guidelines setting the structure and use of reserves.

Budget

Given the discussion above, staff recommends that the Commission adopt the Final Budget and Resolution as indicated in Attachments D and E of this report. The changes between the Proposed Budget and the one discussed in the April report are still valid:

- Fund Balance (Carryover from current fiscal year into FY2009-2010) – The carryover amount was adjusted after re-evaluating some expenses and using the Operating Contingency to cover the additional costs associated with the audit, assuming the Commission approved the contract in Item #2D of this agenda. At $79,034, the Fund Balance is $626 higher than in the Proposed Budget.
- Employee Costs – The Proposed Budget did not take into account the higher costs associated with a higher vacation accrual rate by the permanent staff because of their tenure. This resulted in an increase of $1,500 in Accrued Leave. In order to partially offset the cost, the Executive Officer will have five (5) days of unpaid furlough leave. This resulted in an $850 reduction in salary and PERS contribution costs. However, Employee Salaries and benefits are still $642 higher in this revised budget than in the Proposed Budget.
- General Liability Insurance – At the time the Proposed Budget was approved, the Commission authorized the Budget Ad Hoc Committee to review the various quotes received by this agency on general liability insurance. At the March 25, 2009 meeting, the Commission voted to pursue a contract with the Special District Risk Management Association. The first year's cost for general liability insurance is $3,700, which is $300 lower than in the proposed budget.
- Annual Audit – The allocation for the audit was increased by $200 to partially offset the higher costs associated with the Matson and Isom contract, assuming the Commission's approval was obtained in Item #2D. The Operating Contingency will cover the remaining $2,800 difference between the contracted rate and budgeted amount.

The difference added to the budget in Attachment D is the addition of the proposed reserve. In summary, the budget before you looks like this:

Budget Year	**FY 2008-09**	**FY 2009-10**
Employee Expense	$313,010	$314,349
Operating Expense	$101,100	$97,326
Reserve	$0	$20,000
Operating Contingency	$10,110	$9,733
Expense Total	**$424,220**	**$441,408**
Non-Agency Revenues	$7,344	$8,881
Agency Contributions	$335,749	$353,493
Fund Balance From Prior Year	$81,127	$79,034
Revenue Total	**$424,220**	**$441,408**

For further detail on the calculations or methodologies for deriving these line items other than the items discussed in this memo, please refer to the February 25, 2009 Draft Budget Staff Report (February meeting agenda item #5) and to the April 22, 2009 Final Budget Staff Report (April meeting agenda item #4).

Attachments

Attachment A: Larry Costello's Synopsis of GLI Coverage Comparison
Attachment B: Letter from SDRMA Regarding GLI Coverage
Attachment C: Approved Work Plan, FY 2009-10
Attachment D: Revised Proposed LAFCO Budget FY 2009-10
Attachment E: Draft LAFCO Resolution L-2009-05