



MEMORANDUM

TO: Maryland Counties, Municipalities, and Others Operating Landfills

FROM: Michael Sanderson, Executive Director, Maryland Association of Counties (MACo)

RE: Potential Expansion of MACo OPEB Trust Structure to Landfill Post-Closure Reserves

Executive Summary

- Law change in 2016 gives political subdivisions the authority to invest Landfill Post-Closure Reserves in a manner consistent with funds set aside for other long-term obligations like pensions and OPEB.
- As the sponsor of the MACo Pooled OPEB Trust (the “OPEB Trust”), MACo already has in place a team of consultants and advisors that is working well together and delivering strong performance.
- MACo is, therefore, best situated to offer a full-service, turnkey solution to investing Landfill Post-Closure Reserves.
- Opportunity for early adopters to shape/optimize the structure of the new Landfill Post-Closure Reserves Trust to suit their needs.
- Landfill Post-Closure Reserves Trust to start spring 2018 – stay tuned for updates from MACo regarding a kickoff meeting for interested parties.

Background

Senate Bill 631, enacted into law by the approval of Governor Hogan as Chapter 568, effective October 1, 2016, extends to political subdivisions the ability to invest funds set aside for Landfill Post-Closure Reserves in a manner identical to pension and OPEB funds. With the support of the MACo Board of Directors, I have asked Davenport & Company, Administrator of the OPEB Trust, to assess the merits of setting up a pooled fund similar to the OPEB Trust to facilitate investments by state agencies, counties, and municipalities operating landfills.

Currently the vast majority, if not all, of the reserves set aside for post-closure landfill care are being invested as regular public funds, subject to the typical safeguards and limitations of the investment of such assets, prioritizing safety and liquidity over investment return. The enactment of Chapter 568

allows political subdivisions significant ability to better match the investment of Landfill Post-Closure Reserves to the expected timeframe of their usage; a longer time horizon for use of these funds is consistent with funds set aside for other long-term obligations such as pensions and OPEB. This allows for reserves to be invested in a diversified portfolio of equities and fixed income with an expected long-term investment return in excess of a shorter duration public funds portfolio.

Potential Demand for a new Landfill Post-Closure Reserves Trust

The Fiscal Note prepared for SB 631 in 2016 estimated that the aggregate amount of landfill post-closure liability throughout the state was in the range of \$390 million. This figure reflects only liabilities required under accounting rules to be booked by the various localities in the landfill business; it does not purport to reflect the actual amount of cash set aside to fund such liabilities. Anecdotally, in conversations with several counties around this issue, there appear to be 5-10 local governments (plus MES) with cash set aside in the range of \$6-9 million each. Given that the OPEB Trust started with only a handful of members and roughly \$15 million in initial funding, it seems possible to start a new Landfill Post-Closure Reserves Trust with a similar startup profile.

Using the Existing MACo OPEB Trust Infrastructure Makes Sense

As mentioned above, the amount of reserves set aside by any individual political subdivision is relatively modest. For local units, establishing an investment vehicle on their own for these funds is a sizable amount of work for local staffs. Moreover, investment costs may be prohibitive given the amounts involved.

All of the services provided by the OPEB Trust are relevant to the Landfill Post-Closure Reserves Trust. The key service providers to the OPEB Trust were all competitively procured. Therefore the MACo professional services team is in an ideal position to offer a “turnkey” solution to investing Landfill Post-Closure Reserves, thus saving staff time and creating economies of scale for local participants. In addition, those service providers to the OPEB Trust that are compensated based upon the size of assets under management have agreed to treat the balances in both the OPEB Trust and the Landfill Post-Closure Reserves Trust jointly for purposes of determining their fees.

In other words, if the \$30 million balance in the OPEB Trust were added to a theoretical \$30 million opening balance in the Landfill Post-Closure Reserves Trust, the providers would treat it as \$60 million under management. Fees would be adjusted downward accordingly, benefiting both the OPEB Trust and Landfill Post-Closure Reserves Trust participants regardless of whether they participate in either or both trusts. For purposes of calculating asset-based fees, the Landfill Post-Closure Reserves Trust will be treated as if it has \$30 million in assets before it is funded with the first dollar. Despite being entirely separate entities each with unique asset and liability structures, the Landfill Post-Closure Reserves Trust and the OPEB Trust will reap the cost savings associated with the combined assets of both funds.

MACo OPEB Trust Team Current Governance and Performance

Potential participants in the new MACo Landfill Post-Closure Reserves Trust will naturally want to have an understanding of how the current OPEB Trust is being run and its track record to date. The first investments in the OPEB Trust occurred in April 2015. Assets in the OPEB Trust are currently about \$30 million, representing a doubling in the size of the OPEB Trust during that time. Growth has come from both the addition of new members and investment returns.

Through December 31, 2017, the OPEB Trust has returned 7.1% per year since inception, ahead of the investment return assumption of 7% and slightly behind the custom benchmark return of 7.2%. The difference is largely attributable to the Trustees' conservative approach of dollar cost averaging new contributions over three monthly installments. This decision has protected the OPEB Trust in periods of market weakness, and caused a slight drag on performance. When viewed on a risk-adjusted basis, the OPEB Trust has achieved 101% of the investment return assumption and 98% of the benchmark investment return while experiencing just 73% of the benchmark volatility. The Board meets with the professional services team quarterly and has repeatedly considered and expressed comfort with this trade off.

The OPEB Trust competitively procured the services of GYL Financial Synergies ("GYL") to serve as Investment Advisor. In addition to serving the OPEB Trust, for the past decade GYL has served as advisor to the MABE OPEB Trust serving school systems within the state. GYL has served as investment advisor to other Maryland entities for more than two decades. The firm currently consults to in excess of \$5 billion in assets. Based in West Hartford, Connecticut, GYL also has full-time senior staff in both Kensington, MD, and Richmond, VA. Despite its national client base, GYL's commitment to professionalism and client service is evidenced not only by the attendance of its key principals at MACo OPEB board meetings but also at numerous ad hoc meetings and events. The OPEB Trust also competitively procured custodial services, selecting Wilmington Trust. The Board believed that if they wanted to make a change to Investment Advisor in the future, having a custodian separate from the investment advisor would make for a cleaner switch.

Additional professionals serving the OPEB Trust include legal counsel McGuireWoods LLP in Baltimore which prepared all of the foundational OPEB Trust documents; and Davenport & Company LLC in Towson, which serves as Administrator to the Trust, facilitating meetings, OPEB Trust operations, and accounting/audit functions. MACo's Executive Director serves as an ex-officio Board Member and has the responsibility and authority for certain tasks delegated by the Board. This team of professional consultants now has three years of experience running the pooled OPEB Trust for MACo and is well prepared to take on the Landfill Post-Closure Reserves Trust initiative. The team has a collaborative working relationship with each other and the MACo organization. In 2017, several members of the professional services team led an extensive educational session on fiduciary best practices at the Maryland GFOA Annual Conference.

Implementation Considerations

Landfill Post-Closure Reserve investments and OPEB Trust investments are similar in that they generally serve to pre-fund liabilities with long time horizons before the assets are anticipated to be used to meet their obligations. However, landfills are different in the sense that some have much shorter time horizons until funds will be needed. It is also true that solid waste disposal practices and regulations can change more frequently than OPEB benefits.

For example, most governments evaluate their OPEB liabilities and work through a series of changes, with many reducing the benefit or closing it off to new employees. Once this work is done, the liability and funding streams are fairly well known and predictable. By contrast, solid waste management is often a changing and competitive landscape, with localities choosing to change tipping fees often to manage flow, deciding to keep or transfer waste, or canceling/renewing hauling contracts. Some or all

of these factors can change the post-closure liability picture. Therefore, a MACo Landfill Post-Closure Reserves Trust must have the flexibility in investment approach and ability to add or remove funds as needed in order to meet the timing of the needs of the participants.

The intent of MACo and the professional services team is to bifurcate the Landfill Post-Closure Reserves Trust in an effort to provide liquidity and stability of principal for members' near-term needs while providing for long-term growth of principal to fund long-term landfill closure obligations. There are a variety of ways the Landfill Post-Closure Reserves Trust could be set up and early adopters with significant assets to contribute will have a voice in formulating the structure.

Legal Considerations

Maryland State law does not require the establishment of a trust fund. However, a trust fund structure is permitted under the State law and would provide a pooled investment fund with separate accounts for each participant. The trust fund structure would provide certain efficiencies, namely, the OPEB Trust Fund documents could be used as a model, with appropriate revisions to reflect the differing nature and use of the Landfill Post-Closure Reserves. Input will be requested from potential participants regarding any unique structuring requirements they may have under applicable federal, state, and local law, as well as applicable accounting standards, and the trust fund documents will be modified accordingly.

Next Steps

Based on the expressions of interest conveyed at the November 17, 2017, Budget and Finance Officers workshop at MACo, there seems to be considerable interest in establishing a new MACo Landfill Post-Closure Reserves Trust. This memo is intended to be shared with elected officials and other stakeholders to gain support for establishment of the trust. MACo envisions a meeting of interested parties in late February or March 2018 to review implementation strategies. We will have available legal and investment advisors to answer questions from participants, with the goal of developing a Trust Fund for the investment of Landfill Post-Closure Reserves by the end of March or shortly thereafter. As with the OPEB Trust, there will likely be local board/council action required to formally join the new fund, so initial investments may not occur until later in 2018 as these legislative processes play out. MACo, Davenport, GYL Financial Synergies, and other OPEB Trust advisors will be available to make board presentations in support of moving this initiative forward.