



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Kerrie Romanow
Jennifer A. Maguire

SUBJECT: SEE BELOW

DATE: April 9, 2012

Approved

Date

4/12/12

COUNCIL DISTRICT: Citywide

SUBJECT: COMMERCIAL SOLID WASTE FEES AND MAXIMUM CUSTOMER RATES

RECOMMENDATION

- (a) Approve an ordinance to amend Chapter 9.10 of Title 9 of the San José Municipal Code to amend sections 9.10.1435 to require the exclusive solid waste franchisee to pay a Source Reduction and Recycling Fee (AB939 Fee).
- (b) Adopt a resolution to amend the Schedule of Fees and Charges (Resolution No. 72737 as amended) to revise the Source Reduction and Recycling Fee (AB939 Fee) for commercial solid waste collected city-wide for two exclusive franchise districts at \$4,200,000 per fiscal year to be paid by the exclusive franchisee.
- (c) Adopt a resolution fixing and determining Maximum Commercial Solid Waste Services Rates in the City of San José pursuant to the Commercial Solid Waste and Recyclable Materials Collection Franchise Agreements between the City of San José and Allied Waste Services of North America, LLC dba Allied Waste Services of Santa Clara County, including the total processing costs for organic processing services.

OUTCOME

Approval of the recommendation will ensure that the City has the necessary authority to collect fees needed to fund the management, oversight, and enforcement of commercial solid waste activities.

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BACKGROUND

The City currently issues non-exclusive franchises for the collection of mixed recyclables, organics and garbage from the commercial sector. The commercial sector includes all commercial, industrial and institutional waste generators. An AB939 Fee is assessed on commercial solid waste generators (businesses) and is collected and remitted to the City by the solid waste collector (commercial franchised hauler). This AB939 Fee is based on the volume of garbage collected. Reduced garbage amounts in recent years (due to both the sluggish economy and increased recycling activities) have led to decreased AB939 Fee revenue – from \$2,900,000 in 2007-2008 to an anticipated \$2,000,000 in 2011-2012. Under the current commercial solid waste AB939 Fee structure these declining garbage amounts result in reduced ability to fund required programs. A more stable funding method was incorporated into the final franchise agreements with Allied Waste Services of Santa Clara County (now known as Republic Services, their parent company), approved by the City Council on June 21, 2011. The new fee structure in the agreement includes a flat AB939 Fee of \$4,200,000 to be set by Council resolution and adjusted annually.

The agreement with Republic also includes various maximum customer service rates based on the material collected, container type and size, and frequency of collection. These rates were negotiated with Republic to ensure that they would be able to meet their annual revenue requirement. The annual revenue requirement is the amount needed by Republic to fund their cost of operations, including collection equipment and labor, recyclables processing labor and machinery, and compensation paid to the City's contracted organics processor, Zero Waste Energy Development Company (ZWED), which will process food waste and other organics to produce energy and create beneficial compost. The revenue requirement also includes funding needed to pay for government fees such as Franchise Fees and AB939 Fees, and to allow for a profit margin. Because of the time-lag between the submittal of Republic's original proposal and the actual start of service, the agreement includes a formula (based on changes in indices published by the Bureau of Labor statistics) for adjusting both the revenue requirement and the corresponding maximum service rates from 2010 to 2012 dollars.

ANALYSIS

AB939 Fee

To provide the City with the necessary authority to continue to fund commercial solid waste activities, staff recommends amending the Schedule of Fees and Charges to include an AB939 Fee for solid waste collected by the exclusive commercial solid waste franchisee in San José. The AB939 Fee, which would typically be set through the annual Proposed Fees and Charges process, is being brought forward for City Council consideration now because it is a component of the maximum commercial solid waste services rates. Due to the transition to new commercial solid waste services in June, setting maximum rates now enables Republic to notify all 10,000 commercial customers of their rate and service options prior to the July 1 service start date, so that these customers can make informed and timely decisions on the type and level of service needed for their business.

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The AB939 Fee would not be applied until July 1, 2012, when Republic begins providing service as the exclusive franchisee authorized to perform commercial solid waste and recyclable material collection citywide. Non-exclusive franchises will continue to be issued for the collection of materials such as construction and demolition debris and residential clean-out rubbish through the existing franchise authority. It is anticipated that staff will bring forward approximately 17 new non-exclusive franchise agreements for City Council consideration on May 8, 2012.

The California Public Resources Code authorizes the City to collect an AB939 Fee to be used by the City to cover the cost of administering commercial solid waste programs. The total fee revenue of \$4,200,000 covers the costs for City administration allowing it to operate at 100% cost recovery in 2012-2013. This amount is consistent with staff's original estimation of \$4,200,000 presented to City Council on April 5, 2011, as part of the recommendation to award the exclusive franchises to Republic. This fee represents approximately 7.7% of the total rate charged to customers by Republic for solid waste services and will fund oversight, administration, and enforcement for the City's commercial solid waste system (including the Republic Services and ZWED agreements, as well as the 17 non-exclusive agreements mentioned above), ZWED residue disposal, and other auditing and evaluation required in the Republic and ZWED agreement. The fee will also cover the costs of programs targeted at further increasing waste diversion for the commercial sector, including supporting the development of compostable plastics as part of a larger regional effort, management of public litter cans in commercial areas of the City, and the development of infrastructure to provide business opportunities for diverting hard to recycle wastes.

The City can modify the AB939 Fee as costs change with program modifications, new legislative and/or regulatory mandates, and City personnel cost changes. Given the many new and unique aspects to the redesigned commercial solid waste system (customized collection options for individual businesses, innovative recycling processing technology, the complex interface between Republic and ZWED's processing system for handling organic waste, and the enforcement and related outreach needed to ensure compliance with the exclusive and non-exclusive franchises), the cost estimates for administration and addressing unforeseen circumstances during the first year of service reflect staff's best projection at this time. Many of these costs would likely be limited to the initial roll-out period of the new program. The AB939 Fee will be reassessed in 2012-2013 and modified as needed for 2013-2014, based on an evaluation of actual first-year expenditures for oversight and enforcement of new commercial services.

To facilitate the application of the proposed AB939 Fee to the exclusive franchises, as opposed to the generators (businesses), staff also recommends amending Chapter 9.10 of Title 9 of San José Municipal Code section 9.10.1435. The proposed ordinance would require the exclusive commercial franchisees to pay an AB939 Fee for the commercial waste collected.

Maximum Customer Service Rates

The Republic franchises agreement includes the formula for establishing maximum customer service rates. In late 2011, Republic submitted calculations for adjusting rates for inflationary increases from 2010 to 2012 dollars. Staff verified that the proposed two-year rate adjustment of

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3.846% was consistent with the formula specified in the franchise agreement. This adjustment was based on changes in the Consumer Price Index and an adjustment factor for fuel (compressed natural gas). Similarly, ZWED submitted their adjusted compensation rates (paid to them by Republic) and staff confirmed that the proposed adjustments to the organics processing rates were correct. The organics processing agreement contemplates that proposed organic processing costs would be considered by the City Council. These costs are a component of the maximum commercial collection rates. Due to the transition to new commercial solid waste services in June, setting maximum rates now enables Republic to notify commercial customers of their rate and service options prior to the July 1 service start date, so that these customers can make informed and timely decisions on the type and level of service needed for their business. The proposed Maximum Rates are detailed in the resolution accompanying this report.

In negotiations, the City and Republic developed a customer rate structure that allows Republic to meet their total revenue requirement while encouraging customers to choose cost-effective services that help achieve waste diversion and operational goals. Although businesses may see rate variations on their monthly garbage bill under the new system, rates for the majority of businesses should be similar to current rates and cost competitive with rates charged elsewhere in the Bay Area. However, due to the wide disparity in rates under the current non-exclusive system (where businesses are able to negotiate their rates), the effect on rates will vary widely from business to business. For example, currently, larger businesses with more waste material are often able to negotiate lower rates than smaller businesses with less material.

Although the projections indicate that most rates should not change dramatically, some individual rates for specific service levels may see a considerable increase. The Republic franchise agreement includes a rate balancing process, whereby Republic will work with City staff within six months following initial service to make adjustments to those service levels that see the greatest rate increase, while ensuring that any new rate maximums reflect an appropriate cost for that specific service level. Staff has already solicited the assistance of HF&H Consultants to undertake a rate impact analysis to compare current rates with those in the new system, so that customers likely to be most affected can be identified and rate adjustments allowed for in the Republic agreement can be considered. Concurrently, through review of customer account information, Republic will identify rate categories most impacted and propose adjusted rates for those services. Republic will provide this information to the City to support a request to modify the maximum service rate schedule.

EVALUATION AND FOLLOW-UP

Staff will return to the Council later in May with additional recommended revisions to the Municipal Code to reflect the redesigned commercial solid waste system, including codifying the process to formally adopt changes to the maximum rates in future years. Staff will also report on the transition to the new commercial solid waste system to the Transportation and Environment Committee on May 7, 2012.

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PUBLIC OUTREACH/INTEREST

- Criteria 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

This recommendation does not meet any of the above criteria; however, it will be posted on the City's website for the May 1, 2012 City Council agenda. In March 2012, Republic implemented an extensive outreach campaign to San José businesses, which includes informing customers of new service rates.

COORDINATION

This memorandum was coordinated with the City Attorney's Office and the Office of Economic Development

COST SUMMARY/IMPLICATIONS

The anticipated revenue of \$4.2 million will be included as part of the Integrated Waste Management Fund in the 2012-2013 Proposed Operating Budget scheduled for release on May 1, 2012. This fee will also be presented in the 2012-2013 Proposed Fees and Charges Report scheduled for release early May. The total fee revenue of \$4,200,000 covers the costs for City administration of the commercial program, allowing the program to operate at 100% cost recovery in 2012-2013. This fee represents approximately 7.7% of the total rate charged to customers by Republic for solid waste services and will fund oversight, administration, and enforcement of the City's commercial solid waste system (including the Republic Services and ZWED agreements, as well as the estimated 17 non-exclusive agreements for construction and demolition material and residential clean-out debris), ZWED residue disposal, and cover the cost of programs targeted at waste diversion for the commercial sector (including technical assistance for recycling and outreach, planning, and recycling facility infrastructure development). This fee level also includes the cost of 2.0 Environmental Inspectors that are expected to be brought forward for City Council consideration as part of the 2012-2013 Proposed Operating Budget. The Inspectors will ensure that Republic complies with contractual performance standards, and enforce requirements that no providers are to conduct commercial solid waste and recyclable material collection in San José without a franchise from the City. This enforcement function will

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also help ensure that the cost of the new system will be distributed appropriately among all customers required to participate, mitigating risk of rate increases resulting from Republic not meeting their annual minimum revenue requirement defined in the agreement. It is estimated that related 2012-2013 IWM Fund expenditures will increase by approximately \$245,000 to fund the two proposed Environmental Inspectors. The AB939 Fee will be reassessed in 2012-2013 and modified as needed for 2013-2014, based on an evaluation of first-year expenditures.

The chart below summarizes the estimated 2012-2013 costs that are covered by this fee.

Description	\$	FTE
ESD Personal Services		
Provides for Contract Administration, Commercial Solid Waste program administration, and the portion of management and support staffs' time (ie, personnel, fiscal, budget) allocated to the Commercial Solid Waste program	1,920,000	15.0
ESD Non-Personal/Equipment		
Commercial and ZWED franchise and agreement support and oversight of franchise enforcement program including customer and hauler outreach; process and performance audits required in the agreement.	510,000	
Public Litter Can replacement, maintenance and warehousing	170,000	
Programs targeting additional diversion for waste outside the franchise system (ie., programs promoting reuse and hard to recycle wastes, development of compostable plastics)	170,000	
Support Departments – Personal Services and Non-Personal/Equipment		
Includes Finance, IT, HR, PBCE, DOT, OED, Attorney, and Public Works Personal Services and/or Non-Personal Equipment funding related to activities these departments perform to support the Commercial Solid Waste Program	240,000	2.0
Other Commercial Solid Waste Program Costs		
ZWED Processing Residue Disposal (retained by Republic)	500,000	
General Fund Overhead (Commercial Solid Waste share)	360,000	
City Hall Debt Service (Commercial Solid Waste share)	280,000	
Workers' Compensation Claims	50,000	
Total Costs	4,200,000	17.0

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FISCAL POLICY ALIGNMENT

This recommendation meets the following Budget Balancing Strategy Guidelines from the 2012-2013 March Budget Message: establish a fee structure to assure that operating costs are fully covered by fee revenue and balance ongoing expenditure needs with ongoing revenues to ensure no negative impact on future budgets and to maintain the City's high standards of fiscal integrity and financial management.

CEQA

Not a Project, File No. PP10-067 (a), Increase or Adjustment to Fees, Rates & Fares

/s/

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For questions, please contact Jo Zientek, Deputy Director, Environmental Services Department, at 408-535-8557.