



SAN RAFAEL
THE CITY WITH A MISSION

Agenda Item No: _____

Meeting Date: December 19, 2016

SAN RAFAEL CITY COUNCIL AGENDA REPORT

Department: CITY MANAGER

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City Manager Approval: _____

TOPIC: ANNUAL REFUSE RATE SETTING FOR MARIN SANITARY SERVICE

SUBJECT: RESOLUTION OF THE CITY COUNCIL OF THE CITY OF SAN RAFAEL ESTABLISHING MAXIMUM RATES COLLECTED BY MARIN SANITARY SERVICE FOR REFUSE AND RECYCLABLE MATERIAL COLLECTION AND DISPOSAL SERVICES, TO BE EFFECTIVE JANUARY 1, 2017

RECOMMENDATION:

Adopt the Resolution establishing maximum rates collected by Marin Sanitary Service for Refuse and Recyclable Material Collection and Disposal Services, to be effective January 1, 2017.

EXECUTIVE SUMMARY:

This report details the rate adjustment proposal for 2017 necessary for Marin Sanitary Service (MSS) to provide refuse, recycling and organics composting, hauling, and processing for customers (“rate payers”) in San Rafael. Rate payers include residential homeowners, apartment owners, commercial property owners, and other businesses and tenants. The proposed rate adjustment would increase rates by 5.71% over 2016 levels for all rate payers. It includes adjustments based on an agreed-upon rate setting methodology the City has with Marin Sanitary Service and is based upon an independent third-party review of expenses and revenues by HF&H Consultants, LLC (HF&H).

BACKGROUND:

Each year, the City Council holds a public hearing to set the maximum collection rates that can be collected by MSS in the City of San Rafael. This Background section of the staff report will illustrate the overall context for the rate setting process. In general, the context includes I) the Franchise Agreement and rate-setting methodology with MSS, II) environmental initiatives, goals and regulations, and III) MSS’s services and programs.

FOR CITY CLERK ONLY

File No.: _____

Council Meeting: _____

Disposition: _____

I. Franchise Agreement between City of San Rafael and Marin Sanitary Service

California cities are allowed to regulate local refuse and recycling services under Article XI of the California Constitution and the California Public Resources Code and to collect a franchise fee. The City of San Rafael has a Franchise Agreement with MSS for refuse, organic materials, and recycling collection and services. The revenue-based methodology used to set the annual rates is contained in the Second Amendment to the Amendment and Restatement of Collection Agreement of the City of San Rafael with Marin Sanitary Service (Franchise Agreement) approved by the City Council on October 1, 2012. The Franchise Agreement sets forth the services to be provided by MSS, the rate setting methodology and the franchise fee paid to the City of San Rafael. As required under the current Franchise Agreement, the City Council holds an annual public hearing to set the maximum collection rates that can be charged by MSS for services outlined in the agreement

The Franchise Agreement provides for a detailed third-party review of MSS's operations every three years. In the interim two-year period, annual summary reviews using modified indexes are conducted based on the last detailed analysis. The last detailed review occurred in 2015 for the 2016 rates. The proposed rate levels for 2017 are based on a summary review. This three-year rate setting procedure is the industry-standard for rate-setting for refuse service. As noted in Section V (page 11) of the HF&H report, several expense items are "trued-up" – or adjusted to match actual figures – every year, not just during a detailed review, whereas some items like benefits only get trued-up every third year.

Several jurisdictions in Marin that have contracts with MSS utilizing a similar rate setting methodology have joined together as a Franchisors' Group to share information and reduce costs: San Rafael, Larkspur, Ross, the Las Gallinas Valley Sanitary District, and the County of Marin, including within the Ross Valley Sanitary District boundaries. The Franchisors' Group meets several times per year to oversee MSS's operations, and have met several times since August to review MSS's rate proposals and the work of the consultant conducting the rate review. The results of the rate review are presented in the "Analysis" section of this report.

The 2012 amendment to the Franchise Agreement included many new provisions in order to help stabilize rates, foster zero waste goals, and adjust to changes in the industry and MSS's services. Among those provisions are comprehensive annual reporting to describe progress and achievements in meeting zero waste goals through 1) programs and activities approved by the Franchisors' Group, 2) public education reporting, and 3) reporting on new technologies and industry best practices to enhance progress towards zero waste. Our Franchise Agreement calls for reviewing the contract every five years and revising as necessary, which will be conducted in 2017.

II. Environmental Initiatives and Goals

While perhaps the original purpose of refuse service had to do with public health and safety around sanitation, it is increasingly geared more toward making progress on waste reduction and climate change goals, which are also forms of public health and safety. The State of California has adopted several pieces of legislation mandating significant reductions of waste to landfill, recognizing the embedded environmental impacts and greenhouse gas emissions associated with them.

Consequently, the City's Climate Change Action Plan (CCAP) adopted in 2009, and subsequent Sustainability Element of the City's General Plan, included in 2011, identified eight specific programs under the category of "Reduce Material Consumption and Increase Resource Re-Use," six of which have been implemented to date. Marin Sanitary Service's Food to Energy (F2E) program is an example of one of the programs that has been implemented. In addition, San Rafael is a member of the Marin

SAN RAFAEL CITY COUNCIL AGENDA REPORT / Page: 3

Hazardous and Solid Waste JPA (JPA), which is the group charged with complying with the California Integrated Waste Management Act of 1989. The goal of the Act is to reduce the flow of materials to landfills. The JPA Board is made up of city and town managers and the County Administrator.

The JPA prepared a Zero Waste Feasibility Study in December 2009 which identified a goal of achieving “zero waste in the next five to 17 years.” Zero waste has been defined as 94% diversion of materials from landfill, taking into account the need for producer responsibility and product stewardship, which is beyond local control. The City of San Rafael adopted a Zero Waste Resolution in August 2011 intended to be consistent with the JPA’s goals.

Marin County has a current diversion rate of 74%. The City’s consultant estimated in 2012 that an 85% diversion rate by 2020 will result in an emissions decrease of 22,500 metric tons of CO₂. However, due to the continuing change in materials being produced, diversion rates are often deceptive since they are based on weight. A more accurate means of measuring success might be how much less we are taking to landfill. The JPA and CalRecycle also use a “pounds per person per day” (PPPD) approach in measuring how much landfill trash on average each resident produces. In 2012 the PPPD was 2.78 lbs. and in 2015 that number went down to 2.37 lbs. for rate regulated customers.

MSS and the JPA are putting considerable time and effort into getting organics out of the landfill. The Commercial Food to Energy (F2E) program is in its fourth year and is expected to increase the diversion rate, and new statewide legislation, AB1826, which began mandating commercial composting in 2016, is expected to increase it as well. According to a 2014 Waste Characterization Study, California disposes of approximately 30 million tons of waste in landfills each year, of which more than 30 percent could be used for compost, mulch, and/or energy.

In summary, the overall industry has moved from “bringing garbage to the landfill” to “resource hauling” including transport to recyclers and re-users to find the next highest and best use of materials, with the landfill being the last option. It should be noted that MSS has been a leader in this movement, as they have invested in facilities and technologies to divert materials from the landfill, including the construction of the Marin Resource Recovery Center, Marin Recycling Center, and investments in the F2E program with Central Marin Sanitation Agency.

III. Marin Sanitary Services and Programs

MSS provides residential, commercial and multi-family refuse services, including garbage, recycling and organics collection and processing. MSS also provides trash and recycling pick-up for City facilities, parks, and all sidewalk receptacles throughout San Rafael.

Residential service includes single-family units and three or fewer units in a single structure. San Rafael residential customers receive weekly trash, recycling, and organics composting collection services. MSS added several "Clean-Up" programs to the service offerings in 2016. These included twice yearly residential curbside collections of up to 14 additional bags/cans of yard waste, recycling, and/or garbage; and twice yearly residential on-call collection of up to two large items each time.

Commercial service includes all businesses and residential apartment buildings with four or more units. Commercial customers receive separate trash and recycling containers as well as cardboard pickup, and may choose from a variety of carts, bins, and commercial compactors. In addition, customers are offered the choice of two commercial organics diversion programs. Customers with significant amounts of pre-consumer food waste may participate in the F2E program. Commercial customers with post-

SAN RAFAEL CITY COUNCIL AGENDA REPORT / Page: 4

consumer food waste, food soiled papers, and yard waste may participate in the commercial composting program. All commercial services can be picked up from one to six times per week.

Multi-family buildings are considered commercial services since they are a business enterprise and operate differently than single family homes. They receive separate trash, recycling, and organics containers depending on the area available for can storage. MSS works with apartment managers and tenants to develop 'green teams' to increase recycling and composting at their complexes.

In addition, MSS offers several programs and offerings to the community, including an annual free compost giveaway and community education event. Their staff does the majority of the outreach for the City for the State's Mandatory Commercial Recycling and Mandatory Composting laws (AB 341 and AB 1826). MSS has also assisted with illegal dumping abatement this past year along Jacoby Street at a minimum of once per month. Finally, MSS has a robust community outreach and education program, which provides free resources to customers and schools to encourage recycling and other zero waste activities.

ANALYSIS:

RATE ADJUSTMENT - 2016

In 2016, the Franchising Agencies again selected HF&H Consultants, LLC to conduct the rate review. HF&H has successfully reviewed the MSS rate proposal for several years, and is highly regarded in the industry. MSS reimburses the City and other Franchisors for the consultant's fees for the rate review. Every five years the Franchisors conduct an RFP for future rate reviews, which is slated to take place in 2017.

Over the past fifteen years, the approved annual increases in Marin Sanitary Service rates have ranged from less than one percent to over 10% with an average of 5.19%. Exempting special add-on programs and fees, the average annual increase has been 4.13%. Last year's rate increase was 5.71%.

INITIAL RATE APPLICATION

MSS submitted an initial 2017 rate application in August 2016 as per our requirement, with a proposed 9.91% increase. It is important to note that during each rate review, certain cost categories that were the basis of the prior year rate adjustment are revisited when more actuals based data is available, which can cause increases or decreases to the following year's allowable rate setting projections. For example, if there is a much larger volume of collected materials than was projected, those actual additional costs get added into the following year's adjustment causing an increase that was unanticipated.

EMERGENCY RATE REQUEST FOR RECYCLING

There is a Recycling Reserve Fund established in our agreement with MSS that serves as a rate smoothing mechanism for times when the recyclables market experiences fluctuations. During 2015, there was a sharp decline in this fund primarily the result of the collapse of the commodity markets. Commodity pricing per ton dropped an average of 14.03% during 2015. This collapse is not only being felt in our local jurisdictions, but has been widespread throughout California and the rest of the nation. The existing market conditions are expected to continue in the foreseeable future.

The 2017 rate application also included an emergency request to recover a portion of losses incurred at MSS's recycling center due to a prolonged decline in recycling commodity markets. MSS requested an additional 1.42% to add to the annual rate this year. The Franchisors Group rejected MSS's emergency

SAN RAFAEL CITY COUNCIL AGENDA REPORT / Page: 5

rate request and instead proposed that we negotiate how to address to best address this recycling commodity issue, as well as evaluating the overall rate setting methodology

Our agreement directs the Franchisors' Group and MSS to meet and confer when the Recycling Reserve Fund reaches negative \$250,000, which occurred in 2016. The purpose is to determine a solution which protects both the rate payer and MSS from the negative financial impact of the depressed commodity markets. The Franchisors' Group has agreed to begin discussions with MSS during the first quarter of 2017. MSS's emergency request which they agreed to remove from the current rate application will be addressed during this process. Staff will report back on progress.

ADJUSTMENTS TO RATE APPLICATION

HF&H conducted a review of the MSS rate proposal and recommended adjustments for Franchising Agencies based on allowable expenses in the rate setting methodology, further reducing the rate adjustment by 1.80%. Additionally, MSS refined their projections for 2017 based on the third quarter actuals and a recently renegotiated agreement with Redwood Landfill, and took several steps to further reduce the rate. These steps reduced the rate by .98% as follows: (1) -.22% due to Redwood Landfill renegotiation; (2) -.76% due to updated 2017 operating result projections.

The full rate review and proposed adjustments are contained in the HF&H Report (Attachment C). The following Table breaks out the current rate request components between current year (2017) projected cost increases (2.47%) and the rate impact of prior year (2015/2016) true-up calculations (3.24%), the purpose of which is to reconcile prior year projected amounts with actual amounts realized for a total of 5.71% rate increase for 2017.

Table 2: Rate Adjustment Factor Components

| Rate Adjustment Factor Component Percentages | | | |
|--|--|-----------------------------------|--------------|
| Category | Adjustment Factor Related to 2015 and 2016 | Adjustment Factor Related to 2017 | Total |
| Wages | 0.55% | 0.54% | 1.09% |
| Benefits (including workers comp) | 0.00% | (0.13%) | (0.13%) |
| Fuel & Oil | 1.08% | (0.38%) | 0.70% |
| Disposal | 0.98% | 0.05% | 1.03% |
| Depreciation and Interest | 0.00% | 1.63% | 1.63% |
| Maintenance | 0.00% | 0.11% | 0.11% |
| Other Operating Costs ⁽¹⁾ | 0.33% | 0.07% | 0.40% |
| Subtotal Operations | 2.94% | 1.89% | 4.83% |
| Revenue Shortfall Net of Franchise Fees | 0.30% | 0.58% | 0.88% |
| Rate Adjustment Factor | 3.24% | 2.47% | 5.71% |

⁽¹⁾ Includes profit and general & administrative costs (e.g., public education, customer service, etc.).

ADJUSTMENTS

The following is a brief discussion of the reasons underlying the rate request broken out by major rate categories.

WAGES: This category accounted for 1.09% of the total increase, primarily resulting from the following: 1) MSS filled a key accounting position that had been approved in the 2013 Operational Improvement Plan, but had remained vacant until this past year (0.55%), and 2) increases in overall wages based on the agreed-upon CPI index (0.54%).

BENEFITS: This category accounted for a (0.13%) reduction of the total increase. The above decrease is primarily the result of a reduction in 2017 Worker Compensation insurance costs.

FUEL/OIL: This category accounted for 0.70% of the total increase. This amount consists of the following: 1) a reduction of 0.38% relating to the current year decline in fuel prices; 2) a 1.08% increase related to the impact of prior year true-up calculations. The dollar impact primarily relates to the timing of fuel price changes rather than gallons consumed.

DISPOSAL: This category accounted for 1.03% of the total increase. The majority of the increase (0.98%) is related to prior year true-up calculations. The dollar impact primarily relates to projected and actual tonnage volume.

DEPRECIATION & INTEREST: This category accounted for 1.63% of the total increase. Increases in annual depreciation expense reflect the effects of the decision during 2012 to upgrade and modernize MSS's fleet of collection and recycling vehicles, which are more fuel efficient and use cleaner technology. This modernization was approved and scheduled to take effect commencing in the 2013 rate year. Increases in interest expense reflect the additional financing required to purchase the aforementioned vehicles and equipment.

REVENUE SHORTFALL: This category accounted for 0.88% of the total increase. This is primarily the result of the under realization of projected 2016 revenues which were part of the 2016 rate application process.

RATE PAYER CATEGORIES AND COMPARISONS

With the above recommendation, the cost of a 32 gallon residential landfill cart would be increased approximately \$1.93 per month, from \$32.05 to \$35.81. The cost of commercial service for a 3 yard landfill dumpster picked up once per week would be increased by approximately \$23.90 per month, from \$418.55 to \$442.45. Recycling is included in all accounts. Businesses with a vigorous recycling program can reduce their regular container size or pickup schedule resulting in lower rates.

HF&H conducts a survey of Bay Area refuse haulers as part of conducting the rate review, included in Attachment C. It summarizes the survey data for residential 30-35 gallon can weekly service with curbside recycling and organics pickup. The 2017 proposed rate of \$35.81 in San Rafael is similar to the Marin County average of \$35.46, and the Bay Area average, which is \$34.15. Attachment C also compares the City's three-yard commercial bin (once a week) service to those of all Bay Area cities and agencies with similar services. The San Rafael rate of \$442.45 is slightly higher than the average of other Marin County jurisdictions which is \$401.42, and the Bay Area average, which is \$412.06. However, it is important to note that all jurisdictions provide different services and levels of services,

SAN RAFAEL CITY COUNCIL AGENDA REPORT / Page: 7

making apples-to-apples comparisons problematic. San Rafael's rates have traditionally been comparable with rates in other Bay Area jurisdictions, while often providing more services.

As in previous years, staff is recommending that the rate adjustment be applied across the board to all residential, multi-family and commercial service accounts. Actual rates for all services are provided as an attachment to the Resolution included with this report.

COMMUNITY OUTREACH:

Notice of the public hearing was published twice in the Marin Independent Journal (Attachment B) and mailed to all names on file with the City Clerk. Information on the maximum annual rate that MSS can collect is available at the City Clerk's office during the 10 days prior to the public hearing. The proposed rate information is also provided directly to the San Rafael Chamber of Commerce, the Business Improvement District, Marin Builder's Association, and other interested parties.

FISCAL IMPACT:

The attachment to the Resolution (marked Exhibit C) contains the complete rate request. As shown, the 5.71% overall increase is applied to all customer types and service options. If approved, these rates are projected to satisfy the City's contractual obligations to meet the MSS revenue requirement to cover San Rafael refuse and recycling service costs, including franchise fees.

OPTIONS:

The City Council may choose to:

1. Accept the staff recommendation to institute the maximum MSS rate increases and allocations recommended in the HF&H Report pursuant to the rate setting methodology set forth in the current Franchise Agreement and shown in the attachment to the Resolution effective January 1, 2017.
2. Not accept the findings of the HF&H Report and the staff recommendation and provide additional direction to staff.

RECOMMENDED ACTION:

1. Open the public hearing and accept public testimony;
2. Close the public hearing;
3. Accept the report and adopt the resolution as presented

ATTACHMENTS:

Attachment A: Resolution with Rate Schedule (marked as Exhibit C)

Attachment B: Affidavit of Publication

Attachment C: HF&H Review of MSS Rate Application, including Bay Area Rate Survey