



San Benito County Integrated Waste Management Regional Agency

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June 7, 2023

MEMO: 2023 Recology Exclusive Franchise Solid Waste Rate Adjustment

Dear City Managers and County Administrative Officer,

As you may recall, each year solid waste rates are adjusted throughout the County under the Franchise Agreement between Recology (Contractor) and the Cities of Hollister and San Juan Bautista and the County of San Benito. Integrated Waste Management (IWM) staff has reviewed and has engaged R3 Consulting Group, Inc. (R3) to further review the 2023 rate adjustment calculations submitted to San Benito County (County) by Recology South Valley (Recology). Based on County and Consultant staff analysis and consistent with the methodology in the current franchise agreement approved by the County and both cities, we have confirmed the accuracy of the 5.0% rate increase. The purpose of this memo is to provide a brief overview of the methodology for your discussions with County and City stakeholders and members of the public.

Current 5% Rate Increase effective July 1, 2023

The County and the Cities are members of a Regional Agency (San Benito County Integrated Waste Management Regional Agency) formed to comply with State solid waste requirements and regulations. In 2021, the three member agencies approved a 5-year maximum annual rate increase (not to exceed 5% each year) through a Proposition 218 noticing and rate setting process. A **5.0% increase is effective July 1, 2023** and will be presented in the next Recology residential and commercial bill inserts with no additional need for public noticing or hearings.

Annual Rate Adjustment Background

The current Franchise Agreement was entered into as of November 1, 2018, between the City of Hollister, the City of San Juan Bautista and the County of San Benito, (referred to collectively as the "Regional Agency Members"), and Recology. The annual rate adjustment methodology, found in Attachment E1 of the Agreement, was established in 2018. It utilizes both an index and tonnage-based calculus on the rate components to result in an annual adjustment to the overall rates. As described in the agreement, the multi-index Rate adjustment methodology involves adjusting: (1) the operating component of Rates for the current Rate Period by changes in CPI and Fuel Index; and (2) the disposal, processing, and fee components of the Rates by the actual changes to those components, to determine the Rates for the coming Rate Period.

The intent of performing the multi-index-based adjustment is to allow the Contractor's Compensation to be adjusted throughout the Term of this Agreement (considering those specific cost categories of "fuel" that may be more volatile than the CPI) using simple, readily available indicators of changes in the

Contractor's costs for providing service. The following are the rate components which are adjusted annually, per the Methodology in the Agreement:

- » Operations Component (collection, administration, capital, profit)
- » Disposal Component (local tipping fee)
- » Recycling Processing Component (cost and revenue associated with recyclables)
- » Organics Processing Component (cost to process organics)
- » Fee Component (franchise, AB939, HHW, litter Abatement fees).

The workbook the Contractor submitted showed their calculations. Recology applied the calculated component adjustments to the individual rate components, resulting in new overall rates. Based on County and Consultant staff analysis and consistent with the methodology in the current franchise agreement approved by the County and both cities, we have confirmed the accuracy of the 5.0% rate increase.

The new rates that reflect the 5% increase can be found on www.recology.com/recology-san-benito-county/rates/ beginning July 1, 2023. Should you have any questions, please do not hesitate to reach out.

Appendices included with this memo:

Appendix A - Detailed 2023 Rate Adjustment Components and Findings

Appendix B - Frequently Asked Questions Regarding Recology San Bentio Rates

Appendix A

Detailed 2023 Rate Adjustment Components and Findings

The San Benito Rate Application submitted by the Contractor is comprised of five different sections that when combined totals the overhaul rate increases for commercial, multi-family, and residential customers.

Step 1 & 2 Operating Component (Collection administration, capital, profit): The operating components are costs associated with the collection of materials from residences and businesses, such costs include truck operations and driver labor.

The operating component is a weighted average calculation involving both a standard CPI inflationary index and also a second inflationary component for diesel fuel. Both indexes are derived by the Bureau of Labor & Statistics (BLS). The CPI index is weighted at 94.7%, with the fuel index weighted at 5.3%, with the two comprising of 100% of the Operating Component of each rate.

The CPI inflationary index is calculated based on the Consumer Price Index (CPI) for the San Francisco, Oakland, and Hayward areas. The time period under review was from 2021 to 2022. For the calendar years of 2021 and 2022 the inflationary index was computed at 5.6%.

The fuel index is comprised by the Bureau of Labor and Statistics and is titled "Fuel and related products and powers with a focus on No.2 diesel fuel; the primary fuel source for waste management trucks. For the period under review from 2021 to 2022 the fuel index increased 65.9%.

Combined, the weighted average increases for both inflationary pressures and fuel costs totaled 8.8%. The San Benito Franchise Agreement limits the annual increase derived from the Operating Component to 5.0% annually. Since the adjusted rate increase totals 11.2%, the contractual ceiling of 5% is the correct rate increase as illustrated in Chart 1 – Operations Component Rate Increase. There is a carryover from last year and this year's 5% Operating Ratio cap totaling 6.2% which will be added to future rate increases if the Operating Ratio does not exceed 5% in those years.

Chart 1 – Operation Component of the Rate Increase					
Bureau of Labor & Statistics Index	2021 Index	2022 Index	Annual Percentage Rate	Weight per FA	Adjusted Rate Increase
CPI – San Francisco, Oakland, and Hayward	310.59	327.96	5.6%	94.7%	5.3%
PPI Commodity data for No. 2 diesel fuel	315.92	524.22	65.9%	5.3%	3.5%
2022 Carryforward					2.4%
Total Rate Increase – Operating Component					11.2%
Contractual Ceiling					5.0%

Staff confirmed the accuracy of both indexes used in the San Benito rate application and the accuracy of the math. We also confirmed that the contractual language as defined in the franchise agreement was correctly interpreted by Recology as well.

Step 3 Disposal Component (local tipping fee): The disposal component of San Benito’s rate increase are related to the transportation and disposal of materials into the landfill.

Recology noted no increase in the \$44.75 tip fee from the prior year and did forecast a modest decrease in projected tonnage. The result is a 1.9% decrease in the Disposal Component of the rate increase. Summary results are displayed in Chart 2- Disposal Component of the Rate Increase.

Chart 2 – Disposal Component of the Rate Increase				
Description	Residential	Commercial & Multi-Family Dwellings	On-Call	Total
2022 Tip Fee	\$44.75	\$44.75	\$44.75	
2023 Tip Fee	\$44.75	\$44.75	\$44.75	
2022 Tonnage	13,726	10,441	77	24,243
2023 Tonnage	13,483	10,210	85	23,777
Pct. Change	-1.8	-2.2%	10.4%	-1.9%

Staff confirmed the accuracy of the math. We also confirmed that the contractual language as defined in the franchise agreement was interpreted correctly.

Step 4 Recycling Component (revenue and costs associated with Recycling): The recycling processing component of the rate increase is the revenue and costs related to the transportation, sorting and sales of recyclable materials.

The recycling processing fee per ton increased 16.7% from \$30 to \$35 a ton. The tonnage increase in recyclable materials is expected to grow modestly by 0.3% from 7,946 tons to 7,973.

The franchise agreement does allow liquidated damages for failure to meet annual recycling assessments and annual education and outreach recycling goals. Liquidated damages totaled

\$26K for both 2022 and 2023. Such damages result in a reduction in the overall recycling processing cost and benefit the rate payers.

A second mitigating factor involves performance disincentives. Such penalties occur when minimum diversions level are not met due to too much contamination making materials not suitable for recycling. In the prior year the disincentive value was \$267K and was offset by a \$223K credit. Performance disincentives for 2023 totaled \$124K. Similar to liquidated damages performance disincentives favor the individual rate payer.

The combined increase in tip fee from \$30 to \$35 a ton and then the incorporation of performance disincentives and liquidated damages results in a reduction in costs of 23.4%.

Chart 3 – Recycle Processing Component of the Rate Increase			
Descriptions	2023	2022	Change from 2022
Recycling Processing Fee, per ton	\$35.00	\$30.00	\$5.0
Recycling Tonnage	7,973	7,946	27
Total Revenue			
	\$279,059	\$238,385	17.1%
Performance Disincentive	(\$123,693)	(\$266,792)	143,009
Liquidated Damages	(\$26,401)	(\$26,314)	(87)
Deferral Shortfall Amendment 1		\$223,082	(\$233,082)
Processing Costs net of Adjustments	\$128,965	\$168,361	(-23.4%)

Staff confirmed the accuracy of the math related to the recycling processing component of the rate request. Staff also confirmed that the contractual language as defined in the franchise agreement was correctly interpreted.

Step 5 Organic Processing Component: The disposal component of San Benito's rate increase are related to the transportation and re-use of organic material such as lawn clippings and leaves.

Recology noted a change in the processing fee from \$63.89 to \$67.47 or a 5.6% increase. Organic tonnage is expected to increase 16.2% from 10,495 in 2022 compared to 12,200 in 2023. The increase in processing fees in conjunction with increases in tonnage results in an overall 16.2% increase in organic processing costs across all business lines. Chart 4 – Organic Processing Component of the Rate Increase

Chart 4 – Organic Processing Component of the Rate Increase				
Description	Residential	Commercial & Multi-Family Dwellings	On-Call	Total
2022 Processing Fee	\$63.89	\$63.89	\$63.89	
2023 Tip Processing Fee	\$67.47	\$67.47	\$67.47	
Pct. Change	5.6%	5.6%	5.6%	
2022 Tonnage	9,067	908	520	10,495
2023 Tonnage	9,168	1,593	1,439	12,200
Pct. Change	1.1%	75.3%	177.0%	16.2%
2022 Processing Revenue	\$579,291	\$58,043	\$33,209	\$670,543
2023 Processing Revenue	\$618,539	\$107,474	\$97,112	\$823,125
Pct. Change	6.8%	85.2%	192.4%	22.8%

Staff confirmed the accuracy of the math. Staff also confirmed that the contractual language as defined in the franchise agreement was correctly interpreted.

Step 6 Fee Component: The current rate application includes City and County fees at their existing values (5% and 10%, depending upon the jurisdiction). Because the overall rates went up by about 5%, each of the Fee Components is also escalated by 5%, which is consistent with the franchise agreement language. Staff confirmed the accuracy of the math. We also confirmed that the contractual language as defined in the franchise agreement was accurately interpreted. In conclusion, based upon our review of the calculations, Recology’s submitted rate change calculation was accurately completed.

Appendix B

Frequently Asked Questions Regarding Recology San Benito Rates

Question: How were the Recology collection service rates originally set?

Answer: Recology was the lowest bidder for residential rates on the Request for Proposals (RFP) released jointly by the County of San Benito (County) and the Cities of Hollister and San Juan Bautista (Cities). The other proposers to the RFP were GreenWaste Recovery and RJR Resource Recovery (a new jointly owned firm comprised of RJR Recycling, Atlas Disposal, and Garden City Sanitation). Recology was awarded the franchise in November 2018 and their proposed rates were those adopted at the start of the contract. As part of the negotiation process, staff reviewed and analyzed Recology's proposed rates and costs and negotiated the rates to be lowest possible for the community.

Question: How are Recology's rates adjusted annually?

Answer: The 2018 franchise agreement with Recology obligates the County and Cities to adjust rates annually to compensate Recology for changes in their costs of doing business. There are some cost categories, such as fuel, that may not reflect the sample consumer price index changes. Instead, the rates are adjusted using simple, readily available indices, and some pass-through costs, as follows:

- » Operations Component (collection, administration, capital, profit)
- » Disposal Component (local tipping fee)
- » Recycling Processing Component (cost and revenue associated with recyclables)
- » Organics Processing Component (cost to process organics)
- » Fee Component (franchise, AB939, HHW, litter Abatement fees).

Recology calculates the changes, and the County staff and County consultants review and approve their application administratively. The Agreement also includes a rate cap of no more than 5% per year to further protect ratepayers. The rates may not exceed the rates publicly noticed via the five-year notice for Proposition 218. The proposed rates to be effective July 1, 2023 are substantially lower than the Consumer Price Index change over the past year.

Question: What is the public noticing process?

Answer: In 2021, the three member agencies approved a 5-year maximum annual rate increase (not to exceed 5% each year) through a Proposition 218 noticing and rate setting process. As such, the public has already been notified of the expected rate for July 1, 2023. Recology will present the increase in the next Recology residential and commercial bill inserts with no additional need for public noticing or hearings.

Question: Why is our recycling sent to the ReGen Monterey Materials Recovery Facility (MRF) located in Monterey County, rather than RJR in San Benito County?

Answer: Recyclables processing was a requested service to be provided by the selected hauling company during the RFP process. RJR jointly proposed on the original RFP with two other companies. It is common for companies to compete for collections contracts having arranged for recycling processing via a partnership with a company that they are not direct competitors with. In this case, Recology arranged for recycling processing with ReGen Monterey and ReGen Monterey MRF is an approved facility in the franchise agreement.