



CITY COUNCIL MEETING STAFF REPORT - *Corrected*

Meeting Date: January 21, 2016	Subject: Rate Increase Request by Solid-Waste Franchisee Staff Members: Barbara Jacobson, Interim City Attorney; Mark Ottenad, Public/Government Affairs Director Departments: Legal; Administration	
Action Required	Advisory Board/Commission Recommendation	
<input type="checkbox"/> Motion <input type="checkbox"/> Public Hearing Date: <input type="checkbox"/> Ordinance 1 st Reading Date: <input type="checkbox"/> Ordinance 2 nd Reading Date: <input type="checkbox"/> Resolution Information or Direction <input checked="" type="checkbox"/> Information Only <input checked="" type="checkbox"/> Council Direction <input type="checkbox"/> Consent Agenda	<input type="checkbox"/> Approval <input type="checkbox"/> Denial <input type="checkbox"/> None Forwarded <input checked="" type="checkbox"/> Not Applicable Comments: Solid-waste franchisee Republic Services, Inc., seeks a system-wide 4.4 percent rate increase effective March 1, 2016. This report is a draft version for the Feb. 18, 2016, public hearing for which the City Council may provide direction on issues needing clarification.	
Staff Recommendations: NA		
Recommended Language for Motion: NA		
PROJECT / ISSUE RELATES TO:		
<input type="checkbox"/> Council Goals/Priorities	<input type="checkbox"/> Adopted Master Plan(s)	<input checked="" type="checkbox"/> Not Applicable

ISSUE BEFORE COUNCIL

The City's solid-waste collection franchisee, Republic Services, Inc., is requesting a cumulative, system-wide rate increase of 4.4 percent effective March 1. The questions before Council concern what, if any, rate increase is appropriate and on what effective date?

EXECUTIVE SUMMARY

Solid-waste disposal is regulated by Wilsonville Code (WC) 8.4 and Ordinance No. 204 of 1982 (Ordinance). Subsequent ordinances, some prompted by State mandates, have broadened the service to include the collection of yard debris and recyclable materials. Governing Ordinance No. 204, lays-out six (6) factors that the City Council should consider in determining whether or not to grant the Franchisee a rate increase. This staff report reviews the six criteria of ordinance

applied to the rate-increase request. An Appendix at the end of this report provides a table of data comparing current 2015 rates with the proposed rates effective in 2016; the table illustrates considerable variance in proposed rate changes based on the customer class and bin size that may be of particular interest or concern to Council.

Republic Services, Inc., is the successor in interest through acquisition of the City's solid-waste collection franchise that is governed by Ordinance No. 204 (1982). Republic Services provides a full-range of solid-waste services, including collection and disposal of garbage, large bulky items, recyclable materials and yard debris. Franchisee was last granted a 4.0 percent rate increase effective August 1, 2013.

ANALYSIS OF REQUEST BASED ON ORDINANCE CRITERIA

Matter Is Appropriately before Council

Solid-waste disposal is regulated by Wilsonville Code 8.4 and Ordinance No. 204, enacted in 1982. Through acquisition, Republic Services is the successor-in-interest to Allied Waste Services, which was the successor-in-interest via acquisition to the original franchisee, United Disposal Service, Inc.

Republic Services submitted the request in writing with supporting data for the rate increase on Dec. 18, 2015, providing the required minimum 30-day timely notice for City Council (Council) consideration for the February 18, 2016, public hearing at City Council meeting; Ordinance section 13.

Ordinance Approval Criteria for Rate Increase

Section 13 of Ordinance No. 204 provides six (6) total criteria that the Council "shall consider" in "determining the appropriate rate to be charged by the Franchisee":

- "1. The cost of performing the service provided by the franchisee;
- "2. The anticipated increase in the cost of providing service;
- "3. The need for equipment replacement and the need for additional equipment to meet service needs; compliance with federal, state and local law, ordinances and regulations; or technological change;
- "4. The investment of the franchisee and the value of its business and necessity that the franchisee shall have a reasonable rate of return;
- "5. The rates in other cities for similar services;
- "6. The public interest by assuring reasonable rates to enable the franchisee to provide efficient and beneficial service to the residents and other users of the service."

This report reviews each set of criteria and provides a recommendation.

1. The cost of performing the service provided by the Franchisee.

The Franchisee describes on page 2 of the Dec. 18, 2015, cover letter (Attachment A) the four primary factors that impact the cost of performing the service provided, including "(1) transfer, transport, landfill disposal and waste recovery, (2) Metro's Regional System Fee and Excise Tax, (3) DEQ fee and (4) City of Wilsonville's Host [franchise] Fee."

The Franchisee has provided a proforma Statement of Income [and Expenses] and proforma Schedule of Direct Expenses showing that the cost of operations has increased from \$3,737,049 in 2014 to \$3,771,210 in 2015, which is a net increase of \$34,161 or 0.9% in the cost of operations. *See Attachment B, page 3:*

	2011	2012	2013	2014	2015	% Change to 2014	2016 with rate change	% Change to 2015
Revenue	4,655,237	4,902,229	5,141,169	5,167,317	4,994,567	-3.3%	5,215,405	4.4%
Cost of Operations	3,239,916	3,669,471	3,633,454	3,737,049	3,771,210	0.9%	3,926,216	4.1%

The Franchisee’s financial statements indicate that the cost of providing service has increased by 4.1% from 2011 to 2015; however, this timeframe does not appear relevant since a 4.0% rate increase was granted during the interim in August 2013. The time to start the clock on measuring the change in cost of performing the service would appear to be from the date of the last rate increase, August 2013, rather than an arbitrarily chosen timeframe. Thus, 2014 serves as the only full-year of baseline data. *See Attachment B, page 3.*

Interestingly, in contrast to the cost of operations, Franchisee’s revenue has been flat or declining. Given record single-family home building for three consecutive years primarily in the Villebois neighborhood, which implies an increasing number of customers in greater density, one would expect revenues to increase. For example, during calendar year 2015, the City added 360 new service locations to the City’s utility billing database; while not dispositive of the solid-waste “utility” market, the number is an indication of an increasing number of new residences in the City needing all utility services.

There may be other factors that impact Franchisee’s revenues, such as declining commercial or industrial customer demand. However, given that the Great Recession ended a sometime ago—U.S. National Bureau of Economic Research states that the U.S. recession began in December 2007 and ended in June 2009—and City commercial and industrial vacancies are down considerably from the recession, one would anticipate that commercial and industrial demand for solid-waste services would rebound along with the rest of the economy.

Franchisee has indicated that in meetings with staff that the global collapse of recycled materials markets has significantly negatively impacted revenues, which the rate increase is designed to help ameliorate: “The purpose of this request is...to recover the negative expense incurred to deliver recyclables to markets.” Attachment A, page 1. Based on the Schedule of Direct Expenses, the cost “incurred to deliver recyclables to markets” is *not listed* as a specific expense, and therefore the precise impact on expenses is unclear; Attachment 2, page 4.

The table below shows the change in revenue over the past five years; Attachment B, page 3:

Statement of Income	2011	2012	2013	2014	2015
Revenue	\$ 4,655,237	\$ 4,902,229	\$ 5,141,169	\$ 5,167,317	\$ 4,994,567
Change from prior year:					
• Amount of change		\$ 246,992	\$ 238,940	\$ 26,148	\$ (172,750)
• Percent of change		5%	5%	1%	-3%

Franchisee’s change in revenue, however, is not one of the listed criteria *per se* that is to be used for evaluating a request for a rate change.

One question or issue that is unclear pertains to what kinds of “expenses” are valid for consideration. Specifically, the issue of income-tax expense on gross profit. Franchisee has reported on the Statement of Income, Attachment B, page 1, an operating margin ranging from 13% to 18.3% of gross income. The amount of income tax a company is assessed can vary, based on organizational structure and other factors such as tax credits; plus, taxes are not filed and or paid in the same year, resulting in a time lag. Ordinance No. 204 that provides for the solid-waste franchise is silent on the matter.

	2011	2012	2013	2014	2015
Revenue	4,655,237	4,902,229	5,141,169	5,167,317	4,994,567
Cost of Operations	3,239,916	3,669,471	3,633,454	3,737,049	3,771,210
Gross Profit	1,415,321	1,232,758	1,507,715	1,430,268	1,223,356
Salaries, General and Administrative	561,135	594,000	590,674	595,263	506,076
Gross Income	854,186	638,758	917,041	835,006	717,280
Provision for Income Taxes	341,674	255,503	366,816	334,002	286,912

Summarized below are calculations regarding gross profit or income before income taxes.

Statement of Income	2011	2012	2013	2014	2015
Revenue	\$ 4,655,237	\$ 4,902,229	\$ 5,141,169	\$ 5,167,317	\$ 4,994,567
Gross Income (Before Taxes)	\$ 854,186	\$ 638,758	\$ 917,041	\$ 835,006	\$ 717,280
Operating Margin	18.3%	13.0%	17.8%	16.2%	14.4%

In researching this issue, staff have learned that a number of jurisdictions across the metro region that conduct an annual solid-waste rate review process—including Washington County and the cities of Beaverton, Gresham, Portland, and Milwaukie—consider only the margin before taxes.

In reviewing prior rate increase requests that were granted in full or part, this issue does not appear to have been raised by staff or public, and therefore may not be appropriate for consideration at this time. The issue does, however, highlight an ambiguity in the three-decades-plus-old current franchise agreement that could be clarified in an updated franchise agreement.

In summary, based on proforma Statement of Income and prior City practice in looking at income as a percentage of revenue, the Franchisee appears to demonstrate the cost of providing the service has increased marginally, by 0.9%, during the approximate two-year period since the last rate adjustment in August 2013.

2. The anticipated increase in the cost of providing service.

The Franchisee anticipates the cost of operations to increase by 4.9%, from \$3,737,049 in 2014 to an estimated \$3,920,342 in 2016 without a rate change. The Franchisee sites in the Dec. 18, 2015, cover letter on page 3 a number of factors that are estimated to impact the cost of doing business to provide the desired service.

In researching this issue, staff has learned that some jurisdictions, such as Clackamas County, do not consider cost projections in setting rates, and rather use only actual, full-year data. The City’s

ordinance governing the solid-waste disposal franchise explicitly allows consideration of this factor — the anticipated increase in the cost of providing service. Thus, the City Council may wish to consider updating the franchise agreement that may incorporate provisions addressing the matter, if deemed appropriate.

The proposed rate increase results in an estimated cost of operations in 2016 of \$3,926,216, which is 5% greater than the costs of operations in 2014. See Attachment B, page 3.

	2014	2015	% Change to 2014	2016 with rate change	% Change to 2015	2016 no rate change
Revenue	5,167,317	4,994,567	-3.3%	5,215,405	4.4%	4,994,567
Cost of Operations	3,737,049	3,771,210	0.9%	3,926,216	4.1%	3,920,342

In summary, the Franchisee appears to demonstrate that the anticipated increase in the cost of providing the service is estimated to increase during 2016 by 4.9% to 5% from 2014.

3. The need for equipment replacement and the need for additional equipment to meet service needs; compliance with federal, state and local law, ordinances and regulations; or technological change.

The Franchisee describes various equipment and operational issues in the Dec. 18 cover letter, Attachment A, pages 3-4. In particular, Franchisee notes the fleet transition underway now from diesel-powered trucks to CNG (compressed natural gas) vehicles that are less costly over time to maintain and operate and offer a more sustainable mode of operations.

Franchisee shows the depreciation expense associated with the acquisition of new equipment in the Schedule of Direct Expenses, Attachment B, page 4. The last full-year reported, 2014, shows depreciation expense of \$213,267, which equates to 5.7% of total operating costs.

	2011	2012	2013	2014	2015	2016 with Rate Change	% Change to 2015	2016 No Rate Change
Depreciation	244,976	187,984	195,097	213,267	235,683	295,075	25.2%	295,075

4. The investment of the Franchisee and the value of its business and necessity that the Franchisee shall have a reasonable rate of return.

Franchisee indicates that it is “targeting an 8.8-percent rate of return based on an annualized 12-month revenue.” Attachment A, page 4.

According to Rick Winterhalter, Waste Coordinator for the Clackamas County Office of Sustainability, Department of Transportation and Development, the accepted, reasonable rate of return in the solid-waste disposal industry is in the 8% to 12% range.

Franchisee provides the following financial information pertaining past, current and projected “rates of return,” or income as a percentage of revenue. See Attachment B, page 3.

	2011	2012	2013	2014	2015	% Change to 2014	2016 with rate change	% Change to 2015	2016 no rate change
Income as a Percentage of Revenue	11.0%	7.8%	10.7%	9.7%	8.6%		8.8%		6.6%

Net income as a percentage of revenue has varied over the past four years between 7.8% and 11%. The Franchisee projects that without the requested rate increase the rate of return in 2016 would be 6.6%, substantially below the target rate of return.

As was noted above under criteria No. 1, The cost of performing the service, there is a question as to which measurement should be the appropriate one to evaluate the rate of return, namely pre-tax gross income or post-tax net income. However, this question does not appear appropriate given a lack of explicit mandate in the solid-waste disposal franchise ordinance and past practice.

The Franchisee appears to demonstrate that the requested rate increase produces an 8.8% rate of return based on the requested rate increase taking place.

5. The rates in other cities for similar services.

The Franchisee has provided information on the solid-waste collection and disposal rates of nearby cities Lake Oswego and Tualatin, which are also served by Franchisee; see Attachment A, pages 5-7.

Franchisee highlights numerous factors unique to each community that influence a given class of customers' rates. These factors include the quantity of customers in a given category (residential, commercial and industrial), the volume and types of waste generated by each class of customer, the frequency of collection, number of customers on a route ("route density"), issues of transportation distance, government fee variations, and even policy preferences by Councils in the various cities.

In terms of residential rates, Franchisee indicates that, *using propriety information*, the average residential rate per customer in the three cities served by Franchisee (Lake Oswego, Tualatin and Wilsonville) is \$27.56; see Attachment A, page 6:

Franchisee Propriety Methodology of Comparative Residential Rates

City	Ave Rate per Customer	Deviation from Average
Wilsonville (proposed)	\$ 27.52	-0.16%
Lake Oswego (approved)	\$ 28.88	4.56%
Tualatin (current)	\$ 26.29	-4.84%
Average	\$ 27.56	0.00%

Franchisee indicates that this table "shows the average rate per customer for comparable residential services. The information enables us to evaluate the comparability of the cost of service for these customers. On the basis of average cost per month, Wilsonville customers will pay less than customers in the other two cities. This is primarily the result of a greater proportion of Wilsonville customers using the smallest 20-gallon cart." Attachment A, page 6.

However, when looking at the actual rates as listed, greater divergence appears. Franchisee indicates that the differences in rates are accounted for in part by variations of the customer classes in each city—the various factors noted on the previous page (enumerated in greater detail in Attachment A, pages 5-6)—as well as other factors such a differences in required fees and diverse Councils preferences for advancing certain public policies, such as encouraging less waste generation that favors substantially lower rates for smaller-sized carts.

Following is table showing a comparison of rates for residential, commercial and industrial customers for 2015, prior to rate increases approved by Lake Oswego in late 2015. The Lake Oswego data appeared in a draft version of the rate request submitted by Franchisee.

2015 Rates	Rates of 3 Cities in 2015			Average of 3 Cities	Wilsonville Variance	
	Wilsonville	Lake Oswego	Tualatin		\$	%
Residential Cart Rates						
20 gallon	\$ 21.84	\$ 18.80	\$ 20.65	\$ 20.43	\$ 1.41	6.9%
35 gallon	\$ 24.54	\$ 24.88	\$ 24.21	\$ 24.54	(\$ 0.00)	0.0%
65 gallon	\$ 32.34	\$ 39.69	\$ 31.93	\$ 34.65	(\$ 2.31)	-6.7%
Commercial Rates						
35 gallon	\$ 16.48	\$ 24.46	\$ 18.18	\$ 19.71	(\$ 3.23)	-16.4%
65 gallon	\$ 26.18	\$ 36.44	\$ 24.72	\$ 29.11	(\$ 2.93)	-10.1%
90 gallon	\$ 32.97	\$ 38.75	\$ 31.00	\$ 34.24	(\$ 1.27)	-3.7%
1.5 yard	\$ 121.00	\$ 150.27	\$ 112.12	\$ 127.80	(\$ 6.80)	-5.3%
2 yard	\$ 158.29	\$ 187.79	\$ 148.63	\$ 164.90	(\$ 6.61)	-4.0%
3 yard	\$ 230.05	\$ 248.13	\$ 206.41	\$ 228.20	\$.85	0.8%
4 yard	\$ 299.68	\$ 311.67	\$ 262.16	\$ 291.17	\$ 8.51	2.9%
6 yard	\$ 441.38	\$ 390.80	\$ 370.18	\$ 400.79	\$ 40.59	10.1%
8 yard	\$ 585.26	\$ 504.10	\$ 465.30	\$ 518.22	\$ 67.04	12.9%
Industrial Rates						
10 yard	\$ 103.88	\$ 110.03	\$ 92.17	\$ 102.03	\$ 1.85	1.8%
20 yard	\$ 103.88	\$ 110.03	\$ 108.68	\$ 107.53	(\$ 3.65)	-3.4%
30 yard	\$ 141.70	\$ 130.01	\$ 125.13	\$ 132.28	\$ 9.42	7.1%
40 yard	\$ 163.38	\$ 149.94	\$ 139.41	\$ 150.91	\$ 12.47	8.3%

Following is a table showing a comparison of rates for residential, commercial and industrial customers for 2016 *that includes the rate increase approved by Lake Oswego in late 2015 and proposed by Franchisee for 2016 in Wilsonville*. Note that the same size carts/containers are used on both the 2015 and 2016 tables; other sizes of carts or containers are available but not show below; for a complete list of all size carts/containers, see Attachment 2, page 13.

2016 Rates	Proposed*/New Rates of 3 Cities in 2016			Average of 3 Cities	Wilsonville Variance	
	Wilsonville*	Lake Oswego	Tualatin		\$	%
Residential Cart Rates						
20 gallon	\$ 23.00	\$ 19.91	\$ 20.65	\$ 21.19	\$ 1.81	8.6%
35 gallon	\$ 25.89	\$ 26.34	\$ 24.21	\$ 25.48	\$ 0.41	1.6%
65 gallon	\$ 34.12	\$ 42.03	\$ 31.93	\$ 36.03	(\$ 1.91)	-5.3%
Commercial Rates						
35 gallon	\$ 25.89	\$ 25.90	\$ 18.18	\$ 23.32	\$ 2.57	11.0%
65 gallon	\$ 34.12	\$ 38.59	\$ 24.72	\$ 32.48	\$ 1.64	5.1%
90 gallon	\$ 39.25	\$ 41.04	\$ 31.00	\$ 37.10	\$ 2.15	5.8%
1.5 yard	\$ 134.19	\$ 159.14	\$ 112.12	\$ 135.15	(\$ 0.96)	-0.7%
2 yard	\$ 175.22	\$ 198.87	\$ 148.63	\$ 174.24	\$ 0.98	0.6%
3 yard	\$ 242.70	\$ 262.77	\$ 206.41	\$ 237.29	\$ 5.41	2.3%
4 yard	\$ 316.16	\$ 330.06	\$ 262.16	\$ 302.79	\$ 13.37	4.4%
6 yard	\$ 441.38	\$ 446.47	\$ 370.18	\$ 419.34	\$ 22.04	5.3%
8 yard	\$ 585.26	\$ 533.84	\$ 465.30	\$ 528.13	\$ 57.13	10.8%
Industrial Rates						
10 yard	\$ 115.00	\$ 117.50	\$ 92.17	\$ 108.22	\$ 6.78	6.3%
20 yard	\$ 115.00	\$ 117.50	\$ 108.68	\$ 113.73	\$ 1.27	1.1%
30 yard	\$ 145.00	\$ 138.00	\$ 125.13	\$ 136.04	\$ 8.96	6.6%
40 yard	\$ 165.00	\$ 159.00	\$ 139.41	\$ 154.47	\$ 10.53	6.8%

6. The public interest by assuring reasonable rates to enable the Franchisee to provide efficient and beneficial service to the residents and other users of the service.

The Franchisee believes that the proposed rates are reasonable to enable the Franchisee to provide efficient and beneficial service to the residents and other users of the service.

A question that the Council may wish to consider in terms of “assuring reasonable rates” pertains to particular proposed rate increases for smaller bin sizes for Commercial customers. See Appendix and Attachment B, pages 12, 13 and 15.

Related Issue for Future Discussion

While not part of the rate-increase request or process, staff believes that Council may wish to consider having staff update the Ordinance that governs the solid-waste disposal and collection franchise the following related issue. Staff made to Council a similar suggestion in 2013 during the last rate increase process by Franchisee. Franchisee has indicated agreement that updating the Franchise is a worthy endeavor that could provide greater clarity to all parties.

Specifically, Ordinance No. 204, is 33 years old (passed in 1982). While subsequent ordinances and resolutions (Ordinance No. 281, 1985; Ordinance No. 424, 1994; Resolution No. 2300, 2009) have enlarged the scope of services and increased the rates, the original Ordinance text still governs. Staff suggests that Ordinance should be updated to reflect newer information and methods of doing business, liability insurance coverage and changes in law and technology.

Additionally, through various mergers and acquisitions, the City has done business with the same franchise-holder for over 30 years. While there appear to be no performance issues with the quality of the Franchisee’s services and Franchisee has served the community well for many years, the City Council may be interested in opening-up the solid-waste franchise for bid at some point in the future in order to be consistent with competitive public contracting laws and objectives.

TIMELINE

The Franchisee has requested a rate increase effective March 1, 2016. Staff believes that providing less than a month’s notice to the Wilsonville customers is not sufficient and that more advance notice to customers would be more courteous, reasonable and appropriate. Staff suggests an effective date that provides customers a reasonable 30–60 days’ notice is more appropriate.

CURRENT YEAR BUDGET IMPACTS

This increase would not impact the current year due to the timing of the effective date, but would increase the revenue estimate for the franchise fee for the following year by approximately \$6,625, raising the amount of projected revenue from about \$149,837 to \$156,462.

FINANCIAL REVIEW / COMMENTS:

Reviewed by: S. Cole Date: 1/8/2016

LEGAL REVIEW / COMMENT:

Reviewed by: B. Jacobson Date: 1/14/16

As noted by Mr. Ottenad and as discussed in 2013 when the last rate increase was approved, the underlying franchise agreement dates back to 1982 and is in need of updating to, at the least, accurately cite to current state law. A new agreement could also address any concerns that the Council may raise with respect to how rate increases are to be requested, documented or justified in the future.

COMMUNITY INVOLVEMENT PROCESS

City staff will advertise the requested rate increase and public hearing through media releases, web posts, social media and the Boones Ferry Messenger.

CITY MANAGER COMMENT

APPENDIX

Comparison of Rates	2015 Current Wilsonville	2016 Proposed Wilsonville	Variance	
			\$	%
Residential Cart Rates				
20 gallon	\$ 21.84	\$ 23.00	\$ 1.16	5.3%
35 gallon	\$ 24.54	\$ 25.89	\$ 1.35	5.5%
65 gallon	\$ 32.34	\$ 34.12	\$ 1.78	5.5%
Commercial Rates				
35 gallon	\$ 16.48	\$ 25.89	\$ 9.41	57.1%
65 gallon	\$ 26.18	\$ 34.12	\$ 7.94	30.3%
90 gallon	\$ 32.97	\$ 39.25	\$ 6.28	19.0%
1.5 yard	\$ 121.00	\$ 134.19	\$ 13.19	10.9%
2 yard	\$ 158.29	\$ 175.22	\$ 16.93	10.7%
3 yard	\$ 230.05	\$ 242.70	\$ 12.65	5.5%
4 yard	\$ 299.68	\$ 316.16	\$ 16.48	5.5%
6 yard	\$ 441.38	\$ 441.38	\$ -	0.0%
8 yard	\$ 585.26	\$ 585.26	\$ -	0.0%
Industrial Rates				
10 yard	\$ 103.88	\$ 115.00	\$ 11.12	10.7%
20 yard	\$ 103.88	\$ 115.00	\$ 11.12	10.7%
30 yard	\$ 141.70	\$ 145.00	\$ 3.30	2.3%
40 yard	\$ 163.38	\$ 165.00	\$ 1.62	1.0%

ATTACHMENTS

- A. Republic Services cover letter to Mayor and City Council, RE Rate Increase, December 18, 2015.
- B. Republic Services, City of Wilsonville 2016 Rate Increase Packet