



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Kerrie Romanow

**SUBJECT: REPUBLIC SERVICES
SOLID WASTE SERVICES
RATES**

DATE: April 30, 2024

Approved

Date

4/30/24

RECOMMENDATION

- (a) Conduct a Public Hearing to confirm that the proposed Maximum Commercial Solid Waste Services Rates for 2024-2025 are consistent with the terms of the Commercial Solid Waste and Recyclable Materials Collection Franchises Agreement between the City of San José and Allied Waste Services of North America, LLC, dba Republic Services.
- (b) Adopt a resolution to increase the Maximum Commercial Solid Waste Services Rates in the City of San José for 2024-2025 by 2.32 percent pursuant to the Commercial Solid Waste and Recyclable Materials Collection Franchises Agreement between the City of San José and Allied Waste Services of North America, LLC, dba Republic Services, including the total costs for organics processing services.

SUMMARY AND OUTCOME

Approval of the recommendation will increase the maximum commercial solid waste service rates for Fiscal Year 2024-2025 by 2.32 percent.

BACKGROUND

Allied Waste Services of North America, LLC dba Republic Services (Republic Services) has an exclusive franchise agreement with the City of San José to provide solid waste collection and

processing services to the commercial sector (the Franchises Agreement).¹ The Franchises Agreement was amended and restated and has a term end date of June 30, 2032. The City also has an agreement with Zero Waste Energy Development Company (ZWED) to provide organics processing services for the organics collected under this system.

Republic Services' Commercial Solid Waste collection program, which serves approximately 8,000 business accounts Citywide, was designed and is required to ensure collected waste is processed and recycled to its highest and best use. Waste is separated into three categories: 1) wet or organic material, such as food waste or plant trimmings, 2) dry material, such as mixed non-organic garbage and recyclables, and 3) customized source separated recycling material, such as cardboard, paper, or glass. Customers choose the bin type(s) which works best for their business and are provided consistent rates across the City, access to a service representative who provides ongoing technical assistance, and online access to billing and service data. The system also provides the City and businesses the opportunity to comply with statewide recycling and organics diversion requirements.

Under San José Municipal Code Section 9.10.1695 and the Franchises Agreement, Republic Services may apply for an adjustment to the Maximum Commercial Solid Waste Services Rates once a year. Under the San José Municipal Code, any request to adjust the existing maximum service rate must be in accordance with the application process, methodology, and other factors specified in the Franchises Agreement. The City Council may also conduct a public hearing to confirm that the proposed maximum service rates are consistent with the terms of the Franchises Agreement. The franchisee must provide all customers with advance written notice of changes to the maximum customer service rates at least 30 calendar days prior to the effective date of the change.

Customer service rates vary based on the material type collected, container type and size, and frequency of collection. The rates are set and adjusted each year to satisfy Republic Services' annual revenue requirement under the Franchises Agreement, which is the dollar amount needed to fund the cost of operations, including collection equipment and labor, recyclables processing equipment and labor, compensation to ZWED for organics processing service, and payment of Government Fees (Franchise Fees and Source Reduction and Recycling Fees) to the City. Per the Franchises Agreement, the revenue requirement also allows Republic Services to calculate its profit for the coming rate year by dividing the anticipated total annual cost of operations for the coming rate year by a set ratio and subtracting the same total annual cost of operations from the result. City staff reviews the commercial solid waste service rates application for accuracy and verifies the numbers against the monthly reports submitted by Republic Services.

Section 10.4 of the Franchises Agreement allows for two rate adjustment methods: index-based or cost-based. Section 10.4.2 of the Franchises Agreement allows the City to request a cost-based rate adjustment at any of the following times: (1) in any year where the index-based adjustment

¹ Republic Services has a franchise to conduct commercial solid waste services in both geographic collection districts in the City, North and South, effectively giving them a Citywide franchise.

results in an increase greater than six percent net of Organics Processing Fee, Government Fee, changes in law, or City-directed scope of work changes; (2) upon request during rate year 16; or (3) at any time when the City desires to use its one-time option. The City opted to use this one-time option for rate year 13, 2024-2025.

The cost-based methodology involves an in-depth review of Republic Services actual cost of operations and operational statistics (staff levels, routes, route hours, etc.) to determine the actual allowable total annual cost of operations for the most-recently completed rate period which forecasts the allowable cost for rate year 13. The intent of performing the cost-based methodology is to examine the actual costs to serve the City's commercial rate payers, instead of continuing to annually adjust the maximum service rates using Republic Services proposed costs from the proposal process as prescribed in the index-based adjustment methodology. The cost-based methodology takes into consideration the impacts of changes in inflation, deflation, number of customers, and service levels of each customer to determine Republic Services allowable compensation and profit.

The adjustment methodologies are designed to protect both the customers and the franchisee by limiting the annual increase allowed and ensuring Republic Services is compensated appropriately as operating expenses fluctuate from year to year. Both the Franchises Agreement and ZWED agreement include annual adjustments.

ANALYSIS

Republic Services submitted a rate adjustment application and proposed a 5.30 percent increase to the 2024-2025 commercial service rates to satisfy its proposed revenue requirement of \$86,663,228. Staff performed a review of the documentation provided by Republic Services for the cost-based rate adjustment and found that several compensation adjustments were necessary. Specific cost components were adjusted in accordance with Section 2.1.1 of Exhibit A to the Franchises Agreement, including profit, organics residue disposal costs, and direct disposal costs. Staff determined that a total revenue requirement of \$84,870,121 is appropriate and consistent with the cost-based rate adjustment methodology described in the Franchises Agreement. These adjustments result in a 2.32 percent overall rate increase to provide the services currently required under the Franchises Agreement. If the City had followed the index-based rate adjustment, it would have resulted in a higher rate increase of approximately 3.58 percent. The results are an approximate annual savings of \$1,045,000 to the rate payers.

As required by Section 2.1.1 of Exhibit A to the Franchises Agreement, actual expenses incurred for rate year 11 (labor related, vehicle related, fuel, etc.) were used as the starting point for calculating the rate year 13 allowable compensation. However, staff found that not all non-allowable/prohibited costs were correctly excluded by Republic Services. Staff, therefore, adjusted rate year 11 costs to remove non-allowable costs for charitable contributions and damages and recalculated expenses to properly exclude the amount.

Pursuant to Section 1.1 of Exhibit A to the Franchises Agreement, Newby Island Resource Recovery Park Processing Costs were calculated by staff as 52,000 tons multiplied by the base rate as adjusted by the United States Bureau of Labor Statistics Consumer Price Index for Urban Wage Earners and Clerical Workers. The ZWED organics residue disposal costs were calculated by determining the lower of a) the actual residue for the City's ZWED tons processed or b) the residue cap of 41.43 percent of the City's ZWED tons processed. Republic Services incorrectly applied the residue cap, and incorrectly added the portion of residue paid by the City instead of subtracting it from the ZWED organics residue processing costs. The Newby Island Resource Recovery Park Processing Costs were, therefore, adjusted and are now proposed at \$10,719,325, an increase of \$84,919 from the previous year. Staff reviewed the Direct Disposal Costs, which are the actual costs to dispose of any material that is not directed to the organics processing contractor or recyclable material processing facility.

Staff also reviewed the calculation of annual direct disposal costs per ton rate and confirmed it agreed with the per ton rate from the applicable time period. Because a discrepancy was found in how the direct disposal tons were determined, staff recalculated the annual direct disposal costs to account for the removal of non-franchised direct disposal tons. Therefore, the adjusted Direct Disposal Costs are \$1,268,526, an increase of \$217,519 from the previous year.

Staff reviewed the method of calculating projected gross receipts and determined that revenue for non-schedule services or minimum lift fees were not included. Republic Services confirmed that revenue from non-franchised areas booked to the larger business unit were properly excluded and no franchised revenue was improperly excluded. Therefore, staff made adjustments to add revenue for non-scheduled services and minimum lift fees.

Staff reviewed the operating statistics and noted that Republic Services is operating above the efficiency level in the original cost forms. Therefore, staff made adjustments to reflect the impact of non-allowable costs, correcting the General and Administrative and container maintenance allocations, removing requested additional costs, and the inflationary impact on these adjustments. For rate year 13, Republic Services' total annual adjusted cost of operations is \$34,649,026, an increase of \$479,072 from the previous year.

The proposed maximum rates, effective July 1, 2024, are detailed in the resolution accompanying this memorandum. In addition to collection services, the 2.32 percent rate increase impacts all associated commercial rates, including bin cleaning, bin locks, pushing and pulling containers into a serviceable position by the truck drivers, and delivery of containers. In accordance with ZWED's contract and the Franchises Agreement, the resolution also includes a cost of living adjustment of 3.9 percent to the rates paid to ZWED by Republic Services for organics processing as allowed in ZWED's agreement with the City. The ZWED portion of the revenue requirement is \$19,235,612, an increase of \$722,030 from the previous year which covers the cost of anaerobically digesting the organic material.

Government Fees equaling \$18,997,632 include a Franchise Fee of \$14,597,632 to the General Fund and a Source Reduction and Recycling Fee of \$4,400,000 to the Integrated Waste

Management Fund. The Franchise Fee is charged to Republic Services for use of City property in providing solid waste services in both San José’s North and South Service Districts; it funds services in the General Fund and may be adjusted each year based on the Consumer Price Index. The Source Reduction and Recycling Fee funds several City functions related to the implementation of the City’s Integrated Waste Management Plan, including oversight, administration, and enforcement of the City’s commercial solid waste system; a portion of ZWED residue disposal; and targeted commercial sector waste diversion programs, including technical assistance for recycling and outreach. The Source Reduction and Recycling Fee may be adjusted each year based on the operating needs of the City and will increase \$500,000 from the previous year, to \$4,400,000 for 2024-2025, as shown in the 2024-2025 Proposed Fees and Charges Report. Overall, the Government Fees portion of the rate increase will be adjusted by \$1,077,624.

The rate application adjustment summary **table**² below summarizes the above rate application adjustments made to calculate the revenue requirement, resulting in the 2.32 percent overall rate increase.

Rate Application Adjustment Summary

	Republic Services Proposed Rate Year 13 (2024-2025) Application	Rate Application Adjustments	Final Rate Year 13 (2024-2025) Revenue Requirement
Annual Cost of Operations	\$28,951,329	-\$564,288	\$28,387,041
Profit allotment to Republic Services	\$4,993,247	-\$97,323	\$4,895,924
Pass-Through Costs	\$1,801,048	\$0	\$1,801,048
Total Cost of Operations	\$35,745,624	-\$661,611	\$35,084,013
Rate Year 12 (2023-2024) Organics Residue Compensation	\$121,465	-\$121,465	\$0
Labor Adjustment for Vacant Positions	\$0	-\$434,987	-\$434,987
Newby Island Resource Recovery Park Processing Costs	\$11,741,121	-\$1,021,797	\$10,719,325
Direct Disposal	\$1,319,765	-\$51,238	\$1,268,526
Organics Processing Fee	\$19,233,415	\$2,197	\$19,235,612
City Fees	\$18,501,838	\$495,794	\$18,997,632
Total Franchisee Revenue Requirement	\$86,663,228	-\$1,793,106	\$84,870,121
Projected Service Rate Revenue at Current Rates	\$82,302,627	\$641,944	\$82,944,570
Maximum Service Rate Adjustment	5.30%		2.32%

² Numbers may not sum exactly due to rounding.

Following the recommended rate increase, the City's commercial solid waste rates will remain lower than average compared to rates charged elsewhere in the San Francisco Bay Area. The **Attachment** – Rate Comparison of Nearby Cities - compares San José's proposed maximum rates for two common service levels with the 2023-2024 rates from nearby jurisdictions. Most neighboring cities will be proposing an increase for their commercial rates (available in May 2024).

EVALUATION AND FOLLOW-UP

The Commercial Solid Waste Franchise Fee and Source Reduction and Recycling Fee are included in the 2024-2025 Proposed Operating Budget which is scheduled to be released on May 1, 2024 and the 2024-2025 Proposed Fees and Charges Report which is scheduled to be released on May 3, 2024.

COST SUMMARY/IMPLICATIONS

It is estimated the Commercial Solid Waste rate increase will generate approximately \$18,997,632 in revenue for the City, which includes approximately \$4,400,000 from Source Reduction and Recycling Fees in the Integrated Waste Management Fund and \$14,597,632 from the Franchise Fees in the General Fund. The additional revenue has been assumed in the 2024-2025 Proposed Operating Budget in the Integrated Waste Management Fund and the General Fund. Proposed increased revenue will fund increased costs related to management and administration of the Franchises Agreement and associated service agreements for the Commercial Solid Waste program that have increased due to external factors.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office and City Manager's Budget Office.

PUBLIC OUTREACH

Republic Services is required to notify all customers in writing of the rate change at least 30 days before the effective date.

This memorandum will be posted on the City's Council Agenda website for the May 14, 2024 City Council meeting.

COMMISSION RECOMMENDATION AND INPUT

No commission recommendation or input is associated with this action.

CEQA

Statutorily Exempt pursuant to CEQA Guidelines Section 15273, File No. PP17-005 Statutory Exemption for Adjustments to Fees, Rates and Fares without expansion of services.

PUBLIC SUBSIDY REPORTING

This item does not include a public subsidy as defined in section 53083 or 53083.1 of the California Government Code or the City's Open Government Resolution.

/s/
KERRIE ROMANOW
Director, Environmental Services

The principal author of this memorandum is Valerie Osmond, Deputy Director, Environmental Services Department. For questions, please contact Valerie.Osmond@sanjoseca.gov or (408) 535-8557.

ATTACHMENT: Rate Comparison of Nearby Cities

ATTACHMENT

Rate Comparison of Nearby Cities

Two common commercial container sizes and prices from several nearby cities in Santa Clara County are shown in the table below. Services included with these rates vary from city to city. Not all cities' rate increases were available as of the date of this memorandum.

Rates are from July 1, 2024 to June 30, 2025, unless otherwise stated.

City	3 Cubic Yard Container Collected Once Per Week (monthly rate)	City	40 Cubic Yard Container (per collection)
San José Current	\$266.53	Santa Clara	\$1,004.00
San José Proposed (Effective July 1, 2024)	\$272.71	Morgan Hill	\$1,063.97
Fremont*	\$283.62	San José Current	\$1,080.29
Milpitas**	\$313.56	Los Altos‡	\$1,103.73
Mountain View	\$385.45	Fremont*	\$1,103.89
Campbell	\$395.23	San José Proposed (Effective July 1, 2024)	\$1,105.35
Gilroy	\$411.31	Cupertino†	\$1,152.74
Santa Clara	\$431.89	Gilroy	\$1,156.22
Palo Alto	\$437.20	Campbell	\$1,206.20
Morgan Hill	\$462.15	Palo Alto	\$1,227.59
Sunnyvale	\$481.70	Saratoga	\$1,254.94
Los Gatos	\$488.91	Monte Sereno	\$1,336.89
Saratoga	\$566.53	Los Gatos	\$1,349.22
Los Altos‡	\$570.21	Milpitas**	\$1,449.96
Monte Sereno	\$579.01	Sunnyvale	\$1,467.07
Cupertino†	\$591.37	Mountain View	\$1,523.85

* From January 1, 2024 to December 31, 2025

** From January 1, 2024 to December 31, 2024

† From February 1, 2024 to January 31, 2025

‡ Includes appropriate level of recycling and organics for no additional charge