



SF Environment
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A Department of the City and County of San Francisco

Edwin M. Lee
Mayor

Deborah O. Raphael
Director

TO: Julia Dawson, Finance and Administration, Public Works
FROM: Jack Macy, Zero Waste Program, Department of the Environment
RE: Special Reserve Fund Report
DATE: October 30, 2015

1. BACKGROUND

The Refuse Collection and Disposal Rate Board (Rate Board) requested in their 2013 Rate Resolution and Order that the Director of Public Works and the Department of the Environment prepare a Report on the Special Reserve Fund (Fund) to the City Administrator and Rate Board no later than November 1, 2015. The Rate Board requested that the Report include but not be limited to: identification of all contributions to and expenditures from the Fund since its inception, including investment proceeds; and a preliminary assessment of future conditions that may require use of the Fund, particularly in connection with the expiration of the City's current Waste Disposal Agreement with Waste Management of Alameda County. If the Rate Board reconvenes on or before December 31, 2015 it may consider this Report at that time.

The 1987 Agreement in Facilitation of Waste Disposal Agreement (Facilitation Agreement) between the City and Sanitary Fill Company (now Recology) required the City, through the Director of Public Works, to recommend to the Rate Board the creation of a Fund to be used for payment of "justifiable extraordinary increases in costs, fees, charges and expenses," resulting from Recology's obligations under the Waste Disposal Agreement, as well as certain costs of hazardous and designated waste disposal, and any other recoverable costs which were not fully covered by the currently effective rates but expected to be recoverable through future rates. This Fund was not to take the place of normal ratemaking processes, but to protect the parties from major fluctuations in the rates that were not anticipated during the ratemaking process and avoid the need for continuous adjustments to the rates. The Rate Board approved the creation of the Fund and the imposition of a surcharge to fund it.

The Facilitation Agreement requires a minimum balance of \$15 million to be maintained through the term of the Waste Disposal Agreement, and until all of Recology's obligations under the Waste Disposal Agreement are resolved and satisfied. The Facilitation Agreement will expire concurrent with the expiration of the Waste Disposal Agreement between the City, Recology and Waste Management of Alameda County for use of the Altamont Landfill. The City expects that the Waste Disposal Agreement will expire in January 2016, when the cumulative tonnage limit in the agreement of 15 million tons is reached. Within five years after the expiration of the Waste Disposal Agreement, the Rate Board must determine whether there is any continuing need for the Fund. If the Rate Board determines that there is no further need for the fund, the Rate Board shall allocate the remaining funds for the benefit of current and future ratepayers. Otherwise, the parties will maintain the Fund until there is no further need for it.

2. FUND CONTRIBUTIONS

The Fund was funded by a 1.3% surcharge on Recology's volumetric billings to residential and commercial customers for service starting November 1, 1988. Recology does not apply a cost-of-living-adjustment (COLA) or make a profit on monies collected for this Fund. All interest earned on balances in the Fund is accrued to the Fund. Investments of the Fund are approved by the City Administrator, which are currently in four certificates of deposit that expire quarterly.

On September 30, 2010, when the Fund had reached nearly \$30 million, the Rate Board ordered that the proceeds from the 1.3% surcharge be reallocated to the Impound Account to offset incurred costs by Public Works for prevention and



management of litter and illegal dumping on City streets, and thereafter, as of October 1, 2010, the 1.3% surcharge was no longer deposited for use in the Fund. In July 2013, the surcharge was discontinued per the Director’s Report and Recommended Orders on the 2013 rate application. From the Fund’s inception through September 30, 2015, the total contributions from the 1.3% surcharge going into the Fund, plus total accrued interest minus all administrative fees, have amounted to a net total of \$38,231,084.

3. FUND EXPENDITURES

The procedures for use of the Fund are established in Attachment E to the 2013 Director’s Report. Requests for expenditures from the Fund are made by Recology. The Director of Public Works makes a recommendation to the City Administrator after the request is reviewed by staff from Public Works, Department of the Environment and the City Attorney’s Office. The City Administrator then makes the determination on the appropriateness of the request. The Director of Public Works memorializes the determination in a Director’s Order. A total of \$8,591,569 has been disbursed from the Fund since its inception. A summary of the disbursements is below:

Date	Expenditure	Purpose	Notes
Feb-95	\$574,181	1994 Alameda County Business License Tax	
Jul-95	\$2,750,000	Allowable pre-1995 regulatory cost recovery	Per the Implementation Protocol for Cost Recovery Pursuant to the Waste Disposal Agreement (Sep-95)
Jul-95	\$1,499,188	Construction costs of the landfill waste water treatment plant	Same as above
Jul-95	\$267,589	Transitional interest on Stage 1 of Subtitle D Waste Cell regulatory costs at the landfill	Same as above
Aug-03	\$383,948	E-waste disposal costs mandated by state legislation	
Feb-05	\$226,112	E-waste disposal costs mandated by state legislation	
Sep-06	\$972,267	Subtitle D landfill regulatory costs from Jan-05 thru Sep-05	
Oct-06	\$966,013	Subtitle D landfill regulatory costs from Oct-05 thru June-06	
Dec-07	\$658,142	Subtitle D landfill regulatory costs from Mar-07 thru July-07	
May-12	\$196,687	Long haul trailer tipper engines at the landfill	
Sep-14	\$97,442	Alameda County transportation & planning fees	
Total	\$8,591,569		

4. FUND BALANCE

The balance in the Fund is equal to the net total put into the Fund of \$38,231,084 minus total expenditures of \$8,591,569, which as of September 30, 2015 is \$29,639,515.

5. ASSESSMENT OF FUTURE CONDITIONS FOR USE OF FUND

The Department of the Environment and Recology’s preliminary assessment of current and future conditions that may require use of the Fund does not identify any specific or potential “extraordinary expenses” associated with Recology’s obligations under the Waste Disposal Agreement in light of the upcoming termination in January 2016 of the Waste

Disposal Agreement. As shown above, the most recent landfill regulatory (Subtitle D) costs reimbursed by the Fund were in December 2007 and the latest equipment (tippers) cost were in May 2012. No additional Altamont Landfill regulatory or equipment costs requiring Fund reimbursement have been identified or are anticipated at this time.

In 2002, Waste Management of Alameda County, Recology, and the City entered into "Amendment Number One to Implementation Protocol for Cost Recovery Pursuant to Waste Disposal Agreement" (Amendment No. 1). In Amendment No. 1, Recology and the City agreed to transfer certain funds to Waste Management and to pay Waste Management an additional \$0.27 per ton disposal charge, and Waste Management agreed to release the City and the ratepayers from any claims for reimbursement of closure/post-closure costs under the Waste Disposal Agreement.

6. NEW LANDFILL AGREEMENT SPECIAL RESERVE FUND

The Department of the Environment executed a new Landfill Disposal Agreement (new agreement) between the City and Recology on July 22, 2015 for use of Recology's Hay Road landfill. This new agreement provides for a new special reserve fund (New Reserve Fund) in an amount not less than \$10 million (in 2014 dollars), as adjusted by the Consumer Price Index, subject to the approval of the Director of Public Works (Director) and if applicable, the Rate Board. The New Reserve Fund may be funded gradually over the first four years of the new agreement. The New Reserve Fund is expected to be funded by a 1% surcharge on all trash delivered from San Francisco to Recology's transfer station or landfill and/or by reallocation of funds from the prior landfill agreement Fund. The size of the New Reserve Fund and/or amount of the surcharge may be changed by mutual agreement of the Department of the Environment and Recology, subject to approval by the Director and if applicable, the Rate Board.

The sole purpose of the New Reserve Fund is to reimburse Recology for costs related to the obligations under the new agreement, which are expected to be recoverable through rates but have not yet been recovered, such as landfill fees. The use of the New Reserve Fund is not intended to take the place of normal ratemaking processes, but to ensure that rates are not subject to major fluctuations that were not anticipated during the ratemaking process and to avoid the need for continuous adjustments to the rates. Expenditures would be approved by the City Administrator, similar to the use of the Fund, under procedures similar to those used for the current Fund. The Director and if applicable, the Rate Board, shall determine whether the New Reserve Fund continues after the term of the new agreement and shall allocate any remaining funds for the benefit of the ratepayers.

7. PROPOSED FUTURE USE OF FUND AND CONTRIBUTIONS INTO NEW RESERVE FUND

The Department of the Environment in consultation with Recology propose the following future use of the current Fund and contributions to and use of the New Reserve Fund:

A) Transfer \$3.75 million from the current Fund, in January 2016, as an initial contribution to the New Reserve Fund. This amount is calculated by the proportion of approximately the first 18 months of the new agreement, from January 2016 through June 2017, divided by the first four years of the new agreement times the \$10 million amount required for the New Reserve Fund. The first 18 months is the duration of the New Reserve Fund before the next anticipated rate change could authorize a 1% surcharge on trash delivered from San Francisco to the transfer station or landfill as the contributions to the New Reserve Fund. Four years is the period that the new agreement allows the New Reserve Fund to be gradually funded toward the required \$10 million. The next anticipated rate process can address how to raise the New Reserve Fund to \$10 million from July 2017 to January 2020.

B) Transfer an additional \$12 million from the current Fund, in January 2016, to the New Reserve Fund. This is the approximate estimated amount that would be used from the New Reserve Fund to reimburse Recology for increased costs incurred, from January 2016 through June 2017, under the new agreement for transportation to and disposal fees at the Hay Road landfill compared to costs approved in the rates for disposal at the Altamont landfill. This reimbursement would cover the increased costs before a new rate is anticipated that could include the increased costs

under the new agreement. The calculation of the estimated \$12 million and the process of reimbursement proposed are as follows:

(1) Recology has developed, and the Department of the Environment has reviewed and supports, a methodology to estimate additional costs of transporting and disposing of materials at the Hay Road landfill. Recology estimates the transportation cost will increase an average \$12 per ton, primarily due to increased labor and truck costs for the additional miles to the Hay Road landfill. This increased transportation cost results in a total projected transportation cost to Hay Road landfill of \$34.96 per ton in RY2016, which approximates the projected cost to Recology's Ostrom Road landfill, plus CPI to 2016, of \$35.44 per ton that was presented in the Supervisor's Budget and Legislative Analyst Report for the previous proposed disposal agreement with Recology. Recology also estimates the disposal cost will increase an average \$9.18 per ton. The disposal cost has fewer components than transportation, so the cost estimate is more precise. The new agreement requires the landfill base tip fee to increase annually by the Bay Area Consumer Price Index (CPI). Recology used the average of the last 5 years of CPI (2.5%) in their estimation of transportation and landfill base tip fee costs. This calculation results in an estimated total increased cost of \$21.18 per ton under the new agreement for the current Rate Year (RY) 2016 (\$12 for transportation and \$9.18 for disposal).

(2) Recology would submit reimbursement requests quarterly with the actual tons disposed in the previous quarter multiplied by the \$21.18 per ton cost increase described above for the period through June 2016, which is the remainder of RY2016. For RY2017 (July 2016 through June 2017) the \$12 per ton cost increase for transportation would be adjusted by the COLA in the previously approved rates and the \$9.18 disposal cost increase would be adjusted by the CPI per the new agreement to determine the new total cost per ton increase that would be multiplied by the actual tons disposed. The Department of the Environment will review the cost calculations and recommend to Public Works for their referral to the City Administrator for final reimbursement approval. Using Recology's projected maximum disposal for mid-January 2016 through RY2017, the total estimated increased cost for reimbursement from the Fund is \$12 million.

C) Retain \$13.89 million in the current Fund, which is the remaining balance after the combination of proposed uses identified above totaling \$15.75 million, not including accrued interest minus fees. This balance would be retained in the Fund until the Rate Board determines there is no further need for the Fund, at which time the Rate Board shall allocate the remaining monies for the benefit of current and future ratepayers. The Department of Environment suggests that the transfer of monies to the New Reserve Fund to achieve the \$10 million funding level would be such a use. The Department of the Environment and Recology believe that balances in both the Fund and New Reserve Fund will be more than sufficient for any potential contingencies and that the proposed uses are to the benefit of current and future ratepayers.

Proposed Future Use of Fund and Contributions to New Reserve Fund through June 2017						
Date	Purpose	Fund Expenditure	Fund Balance	Contributions to New Reserve Fund	New Reserve Fund Expenditure	New Reserve Fund Balance
Oct-15			\$ 29,639,515			
Jan-16	Initial allocation to seed New Fund	\$ 3,750,000	\$ 25,889,515	\$ 3,750,000		\$ 3,750,000
Jan-16 thru Jun-17	Allocation for increased costs under new agreement	\$ 12,000,000	\$ 13,889,515	\$ 12,000,000	\$ 12,000,000	\$ 3,750,000

Note: Figures are approximate and actual balances may be higher with accrued interest minus fees.