



June 14, 2017

Refuse Collection and Disposal Rate Board
Jennifer Johnston for Naomi Kelly, Chair, City Administrator
Ted Egan for Ben Rosenfield, Controller, Member
Michael Carlin for Harlan L. Kelly, General Manager, Public Utilities Commission, Member

Edwin M. Lee
Mayor

Re: Response to Objections to the Director's Report

Mohammed Nuru
Director

Dear Members of the Rate Board:

San Francisco Public Works
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Room 348
San Francisco, CA 94102
tel 415-554-6920

This letter summarizes my responses to the objections that have been filed in connection with the Director's Report and Recommended Orders of May 12, 2017 ("Director's Report"). Under the Refuse Collection and Disposal Ordinance ("Refuse Ordinance"), the Rate Board must rely on the evidence placed in the administrative record during the Director's 2017 hearings through testimony or documents.

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I have organized the objections into eighteen categories, building on a matrix created by the City Attorney's Office, which is included as Attachment A. In the sections below, I have cited those sections of the record that address each category of objection and that support the Director's Report. I will be available during the Rate Board hearings along with staff from Public Works and Department of the Environment (SFE) to address the objections and answer any questions from members of the Board.

1. Rate Increase is Too High (Objections #1, 2, 3, 16, 17, 18)

I agree that the proposed increase of 20% over four years (14.42% in Rate Year 2018, 5.46% in Rate Year 2019, -0.55% in Rate Year 2020, and 0.79% in Rate Year 2021) is considerable and may pose a hardship for some ratepayers. The City has not approved any rate adjustments other than cost-of-living increases since 2013.

The rates are based on Recology's actual costs for services necessary to collect and process residential and commercial refuse. As described in the Director's Report, the largest cost drivers for the rate increases are costs related to business as usual (28%), increased public participation in current programs (24%), implementation of new programs (20%), the higher cost of the new landfill agreement (20%), higher costs related to composting operations (6%), and new capital investments (2%) (Director's Report pages 2-5; Exhibit 86).

The Refuse Ordinance states that rates be "just and reasonable," and requires the Director to review the application and submit a report and recommended orders to the Rate Board. "Just and reasonable" is not a formula or test that the proposed rate must meet to be approved. As noted in the Staff Report (Exhibit 78 pages 5-8), the Director followed a carefully constructed public process. Staff from Public Works, SFE, and consultants, conducted a thorough review of Recology's projected revenues and expenditures, verified detailed information and determined they were generally appropriate, and well documented. The higher cost for expanded collection and processing operations is needed

to move toward the City's zero waste goal (Director's Report; Exhibits 78, 79, and 80). In a number of cases, staff recommended adjustments to cost and revenue projections (Exhibit 78 page 3). I recommended additional changes in the Director's Report (pages 5-8). I am confident that the rates in my Recommended Orders are based on solid evidence and reflect the actual costs for collecting and processing San Francisco's refuse.

2. Rate Increase Is Higher for Apartment Owners with 2-5 Unit Buildings (Objections #52, 53)

Recology's rate increase applies to all residential customers. The 16.4% average projected rate increase includes all residential accounts, not just single family homes (Exhibits 44, 45). Apartment buildings of 2-5 units represent 15% of the accounts within the 1-5 unit category (Exhibit 88). Even with the higher fixed charge, the total cost on a per-unit basis is less than the minimum service for a single family residence because multi-unit buildings can share bins (Director's Report page 10).

A higher than average increase for some customers is the result of structural changes in the rates, increasing the base dwelling unit charge and adjusting bin volumetric charges, toward a more accurate reflection of the cost of service. This rate structure also reflects the operational reality of this industry, in which roughly 60% of the costs of collecting and processing material from customers are fixed. Some differential impacts on customers are an inherent part of rate setting, especially when it is also moving from a focus on volumetric charges on trash bins to a structure that reflects the cost of collecting and processing all refuse streams (i.e., trash, recyclables, and compostables).

R3, a firm with solid waste management industry expertise that served as a financial consultant for Public Works, evaluated Recology's rate proposal as well as other rate structures with different values and ratios of fixed and volumetric charges (Exhibits 79, 87, 88, 89, 90). R3 concluded that the rate structure proposed by Recology produced one of the most consistent and even distributions of customer accounts, with 87% of accounts at or below the 16.4% average increase (Exhibit 68). Another rate option, which kept most customers close to the average increase, but moderated the increase for some customers by reducing the unit charge and increasing the volumetric charges, are the rates that I recommended in my report (Director's Report pages 9-10).

3. Base Service Charge is Too High (Objections #4, 5, 22, 24, 31, 38, 45)

The base unit charge is only one component of a customer's refuse rate. The rates also include volumetric charges for trash (black bins), recyclables (blue bins) and compostables (green bins). A rate needs to be evaluated with all the charges together; it is misleading and inaccurate to assess a single rate component, such as the unit charge, in isolation.

Recology presented an analysis of the fixed versus variable costs of its operations (Exhibit 43). The density and terrain of San Francisco creates a challenging operational environment, with collection costs affected by many variables. Recology's fixed collection and processing costs consist of more than the cost of a truck coming to an address to pick up bins. Recology has overhead and offers a variety of other programs to its customers (Exhibit 1 pages 2-6). In addition to those 32 programs, Recology processes all refuse streams at Recycle Central or Tunnel Avenue before transporting the remainder to other facilities.

By incrementally increasing the unit charge, the City is taking an additional step toward aligning the rates with the fixed cost components of residential and apartment services. A rate structure with a higher unit charge also mitigates the impact of declining trash volumes on Recology's total revenues, as San Francisco increases recovery and moves closer to its goal of zero waste. While the cost of collecting and processing each of the three

streams is comparable and the volumetric charges for recycling and composting service are being increased, these rates are still lower than the volumetric charges for trash service. These lower charges continue to provide an incentive for composting and recycling. Under my Recommended Orders, the volumetric charges for recycling and composting for residential customers are 50% of the cost of an equivalent-sized trash bin.

In recognition of the differential impact of the rates on small quantity waste generators, I recommended a transition credit of \$5 for the first two years for current 20-gallon trash customers (Director's Report page 6).

4. Rate Increase is Unfair to Single Family Residences and 2-5 Unit Buildings (Objections #6, 7, 11, 19, 25, 32, 39, 46)

The increased cost of refuse collection and processing is borne by all customers, not just single family homeowners and 2-5 unit buildings (Exhibit 1A RSS/RGG Schedules B.1-3, F.1). While the unit charge for 6-unit and larger apartment buildings is \$5, the volumetric charges are computed differently – \$24.03 per 32 gallons for trash, recyclables, and compostables, with diversion discounts (Exhibits 1A, 78 page 15; Director's Report pages 10-11). The distribution of the increase for apartment customers is tighter, so more of these customer accounts will experience a rate increase that is closer to the average, but some customers will experience increases that are above and below the average amount (Exhibits 68, 87).

5. Cost-of-Living Adjustment Not Justified (Objections #8,20)

Revising rates using a cost-of-living adjustment (COLA) mechanism is a standard practice in utility rate-making and has been applied to refuse rates in San Francisco since 2001. The formula is tied to known cost increases and published indices, such as the Consumer Price Index, which also fluctuate with the economy. Several of the indices used in the COLA formula are capped. Since the last approved rate adjustment in 2013, the COLA formula has resulted in annual increases of less than 2% each year (Exhibits 46, 47, 61). The City and its financial consultant, R3, performed an extensive analysis of the inflation factors and the COLA formula (Exhibits 78 pages 17-20; Exhibit 79 pages 57-60) and recommended changes to improve the methodology that would be applied in the annual rate adjustment process (Director's Report pages 12-13).

I continue to believe that the COLA mechanism is a reasonable approach to adjusting rates between rate applications. I would also note that in addition to saving ratepayers the cost of more frequent, time-consuming and costly rate applications and proceedings, there is the potential for the COLA to result in a negative adjustment to rates when indices decline. The Proposition 218 notification properly noticed the inclusion of the COLA mechanism as part of the rate application (Exhibit 73).

6. Abandoned Materials Program Should Not Be in the Rates (Objections #13, 30, 37, 44, 51)

While all residences and commercial premises are required to have adequate refuse services, a survey of the abandoned materials collected from San Francisco's streets and public areas suggests that these materials (including mattresses, appliances, electronics, furniture, and other large items or bags of material) come from those same residences and businesses predominantly and are not being brought into the City from other locations. Recology offers many services for customers to discard their unwanted items, including bulky item recycling (bulkyitemrecycling.com) and district cleanup events, yet some customers continue to leave materials on the streets.

The Rate Board affirmed the validity of including the costs of the Abandoned Materials Program in prior proceedings (Exhibits 8, 16). The effectiveness of Recology's management of the program was also demonstrated in a previous report to the Rate Board, including faster response time and greater diversion of

materials from landfill (Exhibit 9). This year, Recology proposes to combine the Abandoned Materials Collection Program with the Bulky Item Recycling Program, which will result in greater efficiencies and lower costs (Exhibit 50). I approved this change, which reduced the number of additional drivers that Recology was requesting for the programs managed separately (Director's Report page 8 and pages 15-16).

A portion of Public Works funding goes to support the Outreach and Enforcement Team (OnE Team), which focuses on reducing illegal dumping with outreach, education, and enforcement. The allocations to Public Works are fully enumerated in the record (Exhibit 55). Recology does not earn a profit on these costs.

7. Zero Waste Incentive Fund Rebates Have Been Misapplied (Objections #20, 30, 37, 44, 51)

Several objectors appear to have misunderstood the issue of "rebates" as reflected in the rate adjustments. In its application, Recology proposed using surplus revenues from two accounts (Special Reserve Fund and Zero Waste Incentives) to offset a portion of rate increase (Exhibits 1A, 49). These funds were collected from all customers (a 1.3% surcharge on volumetric billings for the Special Reserve Fund and an additional 2% operating ratio for Zero Waste Incentives). Recology proposed to apply these excess funds to reduce the rate increase, which would benefit all customers (Exhibits 1A, 49). I concurred that Recology's proposal for the application of surplus revenues resulted in the most efficient and equitable way to use the funds for customers per the procedures governing those funds (Director's Report page 11-12). The gradual drawdown of the Special Reserve Fund mitigates the rate impact over three years (Exhibit 69), builds the new Reserve Fund to the target funding level in lieu of assessing a 1% surcharge to customers, and maintains a balance in the old Special Reserve Fund to protect against unanticipated claims (Exhibit 78 pages 11-13).

8. More Information Needed on Recology's Costs (Objections #14, 21, 28, 35, 42, 49)

Recology's costs are described in detail in the rate application (Exhibit 1A). City staff and an outside consultant reviewed and validated these costs (Exhibits 79, 80).

9. Impact of Zero Waste Incentives on Trash Pickup (Objection #21)

The Zero Waste Incentives do not impact the planning or health departments. The incentives are set as part of the rate process and designed to reward Recology if it reduces disposal tons. State and City laws dictate health department (DPH) and other agency roles in refuse collection and disposal. SFE, DPH, Public Works and Recology will be meeting again soon to discuss minimum service requirements and how to best handle customers that legitimately do not require one or more components of refuse collection (i.e., recycling, composting and/or trash).

10. Blue and Green Bin Charges Generate Revenue to Cover Costs (Objections #28, 35, 42, 49).

The value of recyclables and compostables recovered from the blue and green bins does not cover their cost of collection and processing (Exhibit 1A). City staff reviewed facility costs and the prices for commodities to ensure Recology is maximizing projected revenues. The revenue that Recology collects from recyclables is enumerated in the application (Exhibit 1A RSF Schedule F.3) and has been verified by City staff (Exhibit 78 page 4). Recycling revenue offsets Recology's processing costs (Exhibit 1A RSF Schedule B; Exhibit 70). The revenue from compost is applied at the composting facilities and used to offset their tip charge.

The City, through SFE, has worked to reallocate refuse collection, processing costs, and other externalities to the producers and consumers of products. This process is called producer and consumer responsibility, extended producer responsibility or product stewardship. It is a slow, complex, political process, primarily facilitated through state and, to some degree, local legislation. There have been some variants of success, such as aspects

of state bills on beverage containers (the bottle bill), electronics, mattresses, carpet and paint (Exhibit 58 page 27), and San Francisco bans (e.g., expanded polystyrene), charges (e.g., checkout bags) and other ordinances (e.g., pharmaceuticals). These efforts have reduced San Francisco refuse rates. SFE is currently engaged in additional state bills and efforts (e.g., Sacramento workshops on printed paper and packaging, and plastics), as well as some more local policies under consideration and will continue to help reassign costs back on responsible parties to the benefit of ratepayers.

11. Landfill Agreement Is Too Long (Objection #10)

California law requires each county to have or provide a strategy for obtaining 15 years of disposal (i.e., landfill) capacity. San Franciscans continue to put material in black bins destined for landfill. This rate process provides additional resources to encourage San Franciscans put recyclables and compostables in the proper bins, process landfill bound material to extract recyclables and compostables, and develop markets for problem materials. Nevertheless, Recology projects that some material will continue to be sent to the landfill (Exhibit 2 page 6, Exhibits 64, 71).

12. Recology's Use of Routing Equipment for Enforcement (Objection #15)

In hearings, Recology described expanding its route management system (Transcript pages 175-194, 224-225). The routing software will improve Recology's operational efficiency and communication with its customers and is not intended to be punitive; rather, Recology will use the improved communication to educate customers and ensure compliance.

San Francisco code requires everyone to keep recyclables, compostables and trash separate, and allows Recology and designated people to look in bins. Recology and SFE have audited bins and provided outreach to customers in a wide variety of ways for many years, and additional outreach resources are funded in this rate and outlined in the record. Cameras are fairly common on refuse collection vehicles and their use is increasing as technology improves. Cameras will help identify major sources of bin contamination to enable Recology and SFE to educate customers, assist them in a targeted way, and provide any needed documentation. Customers causing egregious contamination have also received financial penalties for many years. Cleaning up this contamination increases operating costs at the various processing facilities.

13. Lack of Outreach (Objection #23)

Per the Rate Board's direction in the 2013 proceedings (Exhibit 16), Public Works engaged a Ratepayer Advocate to assist in outreach efforts to facilitate public participation in the process and present the public's views at the Director's hearings. Outreach efforts by the Ratepayer Advocate are documented in the record (Exhibits 22, 82, 102) and included both traditional mechanisms (e.g., neighborhood newspaper ads, dedicated phone line, e-mail) as well as the use of new communication tools such as social media (e.g., Facebook, Twitter). This approach resulted in a broader and more inclusive process than in the past, as shown by the number of "hits" on the Ratepayer Advocate's web page and social media sites, phone calls and e-mails, as well as attendance and participation at more than 60 community meetings (Exhibit 102). Recology also sent the Proposition 218 notification concerning the proposed rate increase to all its billed customers and residential service addresses (Exhibit 73; Transcript page 508).

Public Works recognizes that it cannot guarantee that the outreach efforts will reach everyone who might be interested in the rate increase, despite our best efforts to employ traditional and new outreach techniques and communication mechanisms (e.g., social media). I would note that while there were criticisms of our outreach

efforts again this year, nevertheless the seven Director's hearings were well-attended and public comment was robust at every hearing. In response to the Proposition 218 notice, I received more written protests than in prior proceedings, which indicates that the notification was effective. I would also observe that the objections filed with the Rate Board are coming from a broader cross-section of ratepayers than in prior years, which suggests that there is a greater awareness of the rate application and the Director's proceedings.

14. Landlords Cannot Pass Through the Rate Increase (Objections #18, 26, 33, 40, 47)

The ability of landlords to pass through costs as part of rent is not within the jurisdiction of the refuse rate setting process.

15. Recology is a Monopoly (Objections #29, 36, 43, 50)

Recology holds the City's permits under the Refuse Ordinance to collect and transport refuse within San Francisco. The City performed an extensive review, validating costs and revenues projections (see response #1). Recology's allowed profit is set in the rate process, like other regulated utilities.

16. No Senior Discount (Objection #9)

The low-income discount program is not age-related. The Director's Report recommended increasing the income eligibility threshold, potentially increasing the number of individuals who would be eligible for the discount and bringing them into alignment with the low-income programs provided by other local utilities, such as Pacific Gas and Electric and the San Francisco Public Utilities Commission (Director's Report page 19). All customers have the opportunity to right-size their service, if they haven't already done so. Customers are still required to meet minimum service levels. Recology provides some services free of charge, helping customers with disabilities that need extra assistance.

17. Variable Charges Too High (Objections #27, 34, 41, 48)

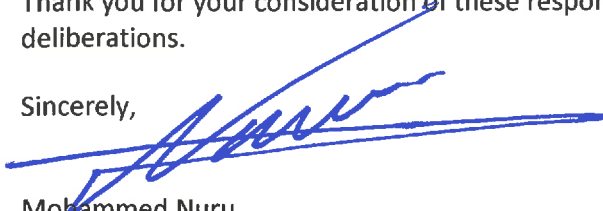
Collection and processing costs are directly correlated with time and material weight. Recology and the City have performed due diligence and researched state of the art technology. Systems that weigh bin contents or determine fullness volume are not sufficiently developed to be used for charging customers. San Francisco is considered a leader in adopting new refuse collection and processing technology. See response #1.

18. Minimum Service and Frequency of Collection (Objections #12, 27, 34, 41, 48)

Weekly collection of putrescible material is required by state law (CCR Title 14, Div. 7, Ch 3, Art. 5, Sec. 17221). In San Francisco, refuse includes recyclables, compostables and trash. Per four interrelated San Francisco codes, dwelling owners are required to have and pay for adequate refuse service, with some exceptions. If after a thorough review process, owners are not in compliance with the minimum service, the City can attach a lien to their property. San Francisco's Mandatory Recycling and Composting Ordinance (Environment Code Section 291) requires everyone to keep recyclables, compostables and trash separate. Approved refuse rates help define minimum service levels. SFE and Recology tested every other week service, pay per set out and smaller trash bins. Smaller trash bins produced the best results with the least amount of contamination between the bins (Exhibit 18; Transcript pages 100-104). In my report, I reduced the minimum trash service for a single family home from 20 gallons to 16 gallons, which will allow many customers to adjust their service and potentially reduce their rates.

Thank you for your consideration of these responses. I look forward to assisting the Rate Board with its deliberations.

Sincerely,



Mohammed Nuru
Director of Public Works

cc: Julia Dawson, Public Works

Deborah Raphael, Robert Haley, Jack Macy, Department of the Environment

Manu Pradhan, Brad Russi, City Attorney's Office

Dwayne Jones, Rosemary Dilger, Ratepayer Advocate, RDJ Associates

Attachment A

Attachment A – Summary of Rate Board Objections by Category

Objection Number	Increase Too High	Base Service Charge Too High	Unfair to SFH and 2-5 Units	COLA	Abandoned Materials Program	More Info Needed	Other	Senior Discount	Bin Size
1. Rate increase too high (<i>Schlatz</i>)	X								
2. Rate increase too high (<i>Lindeboom</i>)	X								
3. Rate increase too high (<i>Bassan</i>)	X								
16. Rate increase is too high (<i>Wong</i>)	X								
17. Rate increase is too high (<i>Sinn</i>)	X								
18. Rate increase is too high (<i>Damm</i>)	X								
52, 53. Rate increase too high, particularly for 2-5 unit buildings (<i>Kramer, Richen</i>)	X								
4. Base service charge too high (<i>Bassan</i>)		X							
5. Basic service charge for single family homes excessive (<i>Bassan</i>)		X							
22. Base charge discriminates against customers with small trash footprint (<i>Laffan</i>)		X							
24, 31, 38, 45. Increase in base rate is too high (<i>Lemmon, et al.</i>)		X							
6. Basic service charge for single family and 2-5 unit buildings unfairly shifts burden from bigger buildings (<i>Bassan</i>)			X						
7. Increase for blue and green bins too high for single family homes and 2-5 unit buildings (<i>Bassan</i>)			X						
11. Homeowners cannot opt out of garbage service. Unfair to place burden on single family homes and smaller buildings (<i>Bassan</i>)			X						
19. Increase to base charge is too high and unfair to 2-5 unit buildings (<i>Laffan</i>)			X						
25, 32, 39, 46. Base rate unfairly discriminates against owners of 2-5 unit buildings (<i>Lemmon et. al.</i>)			X						
8. No justification for COLA adjustments (<i>Bassan</i>)				X					
20. Customers being charged for COLA twice; once with Zero Waste Initiative and once with rate increases (<i>Laffan</i>)				X					

Attachment A – Summary of Rate Board Objections by Category

13. Rates should not include the cost of cleaning up illegal dumping (<i>Bassan</i>)					X				
30, 37, 44, 51. Rate Board should demand information on what charges Recology included in the application to pay for costs by City departments (<i>Lemmon et al.</i>)					X				
14. Customers lack information regarding Recology’s Costs (<i>Bassan</i>)						X			
21. There should be a review of the Zero Waste Initiative (<i>Laffan</i>)						X			
28, 35, 42, 49. Increase in blue and green bins despite revenue generation; should seek an explanation for this (<i>Lemmon et al.</i>)						X			
10. Consumers should not be paying for a 15-year contract (<i>Bassan</i>)							X		
15. Tool to photograph and report improperly sorted bins is improper (<i>Bassan</i>)							X		
23. Outreach efforts for rate application were not effective (<i>Laffan</i>)							X		
26, 33, 40, 47. Director’s ruling conflicts with the Rent Ordinance (<i>Lemmon et al.</i>)							X		
29, 36, 43, 50. Increase represents monopoly pricing by Recology (<i>Lemmon et al.</i>)							X		
9. Recommended low-income discount for seniors is deficient (<i>Bassan</i>)								X	
12. Increasing charges on larger bins will encourage dumping (<i>Bassan</i>)									X
27, 34, 41, 48. Increase for black bins does not recognize that rates should not necessarily increase with bin size (<i>Lemmon et al.</i>)									X