

STAFF REPORT

DATE: November 16, 2021

TO: City Council

FROM: Stan Gryczko, Director, Public Works Utilities & Operations
Adrienne Heinig, Assistant to the Director

SUBJECT: Solid Waste Annual Fund Review/Rate Adjustment Recommendation

Recommendation

1. Receive informational item on the financial status of the City's Solid Waste Fund (520), as presented in the staff report to the Utilities Commission on October 20, 2021; and
2. Approve the resolution (Attachment 1) that the fourth-year rate adjustment for the Solid Waste utility be implemented at 5%, with the adjustment occurring on January 1, 2022.

Fiscal Impact

After a number of years of expenditures outpacing rate revenue in the Solid Waste Fund, the planned adjustments from the last cost of service study have restored balance in the fund. With revenue exceeding expenditures, City staff and the Utilities Commission can shift focus to the delayed fund expenditures and prioritize spending on those items, as well as review the impact of upcoming regulatory changes. Action on rates is essential to ensure that the fund continues to recover, and to smooth out (as much as possible) upcoming rate requirements associated with the implementation of Senate Bill (SB) 1383.

Council Goals

This effort is consistent with the Council Goal to Ensure Fiscal Resilience.

Commission Input

The implementation of utility rate adjustments, either at or below the established Proposition 218-complaint rate schedule, is under the direct authority of the City Council. In advance of this recommendation coming before the Council, the rate adjustment recommendation from staff was presented to the Utilities Commission, as has been the practice for each annual adjustment in this rate schedule. A more detailed summary of the discussion of the Commission is included within this report, however in brief the Commission motioned the following:

Motion: Recommend to the City Council that the fourth-year rate adjustment for the Solid Waste utility be implemented at 5%, with the adjustment occurring on January 1, 2022.

Moved by L Deos, seconded by E Roberts-Musser. The motion passed by the following votes:

Ayes: G Braun, A Cullen, L Deos, S Gellen, L Kristov, E Roberts-Musser,
J Troost

Noes:

Absent:

Background

Approval of Five-Year Rate Adjustments

In February of 2019, after months of discussion with the Utilities Commission and the City Council, the Council approved a five-year schedule of rate adjustments for the Solid Waste Utility. Pressures on the Solid Waste fund, as well as the results from the solid waste rate study conducted in 2019, necessitated the implementation of larger-than-average adjustments to rates to establish fiscal sustainability and a reserve for the fund, which would buffer the fund and ratepayers from future demands of service level changes, regulatory changes, or other adjustments. Prior to the adoption of the rate schedule, staff and Council worked to adjust the recommended implementation dates to further buffer ratepayers from the initial rate adjustments, moving the recommended January 2020 rate adjustment to June 2020. The precarious position of the fund, in the years of recovery, left it more vulnerable to changes in revenue or expenditure than other City utilities, and it was hoped that the initial adjustments would shorten this period of vulnerability to two or three years.

Council Direction in October & December 2020

As part of the City Council direction to return each year with a report on the fiscal health of the Solid Waste fund, and a recommendation for the next year's rate adjustment (within the approved Proposition 218 period of rate adjustments), staff presented a fund update to the Utilities Commission on October 21, 2020, prior to the implementation of the planned 8% rate adjustment in January 2021. This adjustment discussion also included the consideration of the 10% rate adjustment postponed based on Commission recommendation and Council direction in May 2020. The June 2020 10% adjustment was postponed as a result of the COVID-19 pandemic and associated economic impacts. In addition to postponing the 10% adjustment in Solid Waste fees, the City Council also approved an urgency ordinance to in part waive new City utility bill late fees for all residential and commercial customers, allowing late payments without penalty through May 2020. This waiver was ultimately extended to April 2021.

Consideration of the Postponed Adjustment and Fund Performance during COVID-19
Up to April 2020, the Solid Waste fund continued to perform at pace with expectations from the 2019 cost of service study. While the fund expenditures did remain higher than revenue, and the fund balance continued to drop, the amount of the fund balance drop lessened by the end of FY 19/20, as anticipated. This is consistent with the cost of service model showing a decrease in the fund balance until year 3 (2021) of the 5-year adjustment period, when revenue would overtake expenditures and the fund balance would begin to rebuild.

The impacts of a global pandemic, however, disrupted the return to health of the fund. From the report to Council on December 15, 2020:

“Staff have carefully tracked revenue from the utilities since March of this year, to identify any impacts of the actions by Council in March to forgo the implementation of new late fees for non-payment of utility bills, and note that the Solid Waste fund is the only utility fund that has seen appreciable impacts to revenue since the beginning of the COVID-19 pandemic response. Stormwater, Water and Wastewater utilities continue to see actual revenue each month at pace with previous year performance, or slightly higher.”

With revenue losses of \$40,000 on average each month, action was required to assure the health of the Fund, and to avoid incurring further debt. Staff recommended to the Commission in October 2020 that the rate adjustments consisting of 12% on January 1, 2021, and 6% on July 1, 2021 be implemented. This recommendation was supported by the Commission, with one dissent vote, and ultimately approved by Council.

June 2021 Fund Micro-Update

In a memo received by the Commission on June 16, 2021, staff included a short fund update focused on the Solid Waste fund balance. In June, the fund balance was anticipated to be lower than the fund balance calculated in October 2020, based on the reduction in rate revenue with commercial business closures during the shelter-in-place orders at the height of the COVID-19 pandemic.

The fund review for the city’s Solid Waste Fund is included in pages 2-12 in the attached staff report to the Utilities Commission, presented on October 20, 2021 (Attachment 1).

Utilities Commission Review and Recommendations

In the development of the fund review for the Commission, staff noted two important items for consideration. First, the implementation of Senate Bill (SB) 1383, and associated cost impacts, are not specifically included in the model being utilized for the current Proposition 218 schedule. Because of this, forecasting with the current model will not reflect the actual costs of the program moving forward. Second, the Utilities

Commission will be considering a Request for Proposals (RFP) for a Solid Waste Cost of Service study to begin early next year, a study which will assess the probable cost increases associated with the implementation of SB 1383. With that study, the Commission will review the Solid Waste Fund expenditures and revenue in depth over the next twelve (or so) months.

The Commission was presented with a memo prepared by staff, and a brief discussion of the contents of the memo at their October 20, 2021 meeting. As the current schedule is nearly the end of the implementation dates (this discussion is on year four of the five-year schedule), the recent restoration of the balance between expenditures and rate revenues, and the impending implementation of SB 1383, staff did not provide alternative scenarios for the Commission to consider.

Commission discussion on the solid waste fund update and rate recommendation from staff included the following:

- Clarification that the recommendation from staff is only for Jan 2022, consideration will be given to the next adjustment in schedule (January 2023) in October of next year.
- Concern around the debt taken by the fund. With the loan from the wastewater utility being extended from 10- to a 15-year payoff, payments of interest as required have continued, but principal payments have not been able to be made as the fund has progressed toward recovery. Commissioners requested that the payments to the principal loan be made in earnest (and prior to the financial plan discussions with the cost of service study).
- Concern around external contingencies that may impact the fund, including the likelihood of Recology requesting a detailed rate review, and how that review might impact rates moving forward. Staff indicated that external impacts such as rate reviews or tipping fees, etc. would be a consideration of the upcoming cost of service study.
- How utilities are able to provide loans to other utilities, and concern that the true cost of running the utility is not accurately reflected with the loan balance outstanding.
- The timing of rate studies, and how Proposition 218 rate schedules provide boundaries for how jurisdictions can move forward in reviewing the cost of service of the utility.

The Utilities Commission will continue to conduct annual fund reviews of the City's Solid Waste fund, with check-ins at the mid-year should contingencies arise that would impact the Fund in the very near term. As previously stated, the Commission will start the next cost of service/rate study in 2022.

The Implementation of SB 1383

As of the drafting of the December 15, 2020 report to Council, the California Department of Resources, Recycling and Recovery (CalRecycle) had just finalized rulemaking on SB 1383 (Short-Lived Climate Pollutants: Organic Waste Methane Emissions Reductions), despite the implementation date of January 1, 2022. The rulemaking was finalized in November 2020, with the final language of the regulations released in February 2021.

With the release of the final regulations, City staff has been working with consultants, legal teams, internal working groups and County staff to develop implementation plans for SB 1383 compliance both individually by jurisdiction, and collectively as a County (specifically for the development of the edible food recovery program). It should be noted that although the work towards SB 1383 compliance ramped up in early 2021 with the release of the final language, staff have been preparing for the regulations for a number of years.

As a reminder, SB 1383 establishes targets to achieve a 50 percent reduction in the level of the statewide disposal of organic waste from the 2014 level by 2020, and a 75 percent reduction by 2025. The law grants CalRecycle the regulatory authority required to achieve the organic waste disposal reduction targets and establishes an additional target that not less than 20 percent of currently disposed edible food is recovered for human consumption by 2025. The regulations will go into effect by into effect January 1, 2022, with the full implementation of the regulations in place by 2032.

There are a number of items in the regulations that would have impacts on Davis, and utility ratepayers, including the following:

- Changing the labels and lid colors for all Recology Davis collection bins to be complaint with the regulations (current bins do not match the requirements)
- Translate a variety of mandated outreach items to customers in their native language (for any language spoken by 5% of more of our customers)
- New reporting requirements to the state
- City ordinance updates
- Inspections, audits and recordkeeping of organic waste generators, and more

The regulations also include the establishment of an edible food recovery program, however as Council is aware staff is exploring the question of funding associated with this program, and opportunities within social services programs to offset costs.

The implementation of the city-wide mandatory organics collection program in 2016, along with the robust education and outreach program already in place, have put the City in an excellent place both in terms of meeting the requirements of the regulations, and already accounting for a significant cost in the rate structure.

Staff is in the process of reviewing the implementation roadmap with the Natural Resources and Utilities Commissions. An informational item has been provided to the Recreation and Park Commission as an introduction to the regulations, the ordinance updates (in concept) have been presented to the Natural Resources Commission, and the edible food recovery portion of the regulations has been reviewed by the Social Services Commission. The feedback from City commissions on the implementation of SB 1383, along with any recommendations, will be brought to the Council in December of this year.

Staff Recommendation

A rate adjustment of 5% on January 1, 2022

Month/Year	Adjustment	\$ Impact	Rate (SFR) 65 gal
Mar 2019	13.5%	\$0.00	\$38.95
Jan 2021	12%	\$4.67	\$43.62
Jul 2021	6%	\$2.62	\$46.24
Jan 2022	5%	\$2.31	\$48.55
Jul 2023	5%	\$2.43	\$50.93

The staff recommendation was developed with the following goals in mind; 1) to maintain the balance of the fund (with revenues exceeding expenditures), thus relieving the pressure on the fund balance, and 2) to allow for the continued development of the reserve, to provide a buffer against regulatory changes required in the next year. The current approved Proposition 218 rate schedule includes a 5% increase planned for January 1, 2022. With this recommendation, rate payers will see an increase of 5%, and the average single-family customer will pay \$2.31 more for solid waste services in 2022.

The recommendation from staff maintains the balance of the fund around the time originally anticipated, and brings the total fund balance up at a faster pace. With this adjustment, it is also likely that future rate adjustments (outside of the current Proposition 218 period) for the Solid Waste rates should be within previous expectations (around 5% annually), however the rate adjustments recommended might be higher to account for the regulatory changes and deferred payments to the loan or other deferred expenditures. As a reminder, the following assumptions have been made throughout the rate adjustments of this Proposition 218 schedule:

1. The full anticipated adjustment for the Proposition 218 approval period will be implemented. Scenarios which dropped a year of the adjustments demonstrated the action was not feasible to maintain the fund.
2. The scenarios assume that the next rate study would likely result in recommended rate adjustments slightly higher than anticipated with the original recommendations, and would be necessary to maintain the fund and to be able to implement projects and studies beyond basic utility operations.

3. For the remainder of the approved rate adjustment period, planned expenditures for any activities not immediately required for operations by the utility would be deferred indefinitely.
4. The target reserve would likely not be reached within the approved rate adjustment period, and the City would not have any cushion (fund balance above a reserve) to aid in rate impacts associated with the implementation of Senate Bill (SB) 1383. The fund would also not provide a cushion for additional regulatory changes, detailed rate reviews requested by the contract hauler, major emergencies, or other unforeseen financial impacts.

Rates of Surrounding Communities

As included in the memo to the Utilities Commission, in the review of Solid Waste rates of surrounding jurisdictions, 6 of the 12 communities surveyed have raised rates *since October 2020*. Likely this is in preparation for the implementation of SB 1383. Four of the jurisdictions surveyed (including the jurisdiction with the lowest solid waste rates) do not have an organics collection program in place, and will likely see rate increases in the short term to implement the required programs, now that rulemaking is completed.

Next Steps

Should Council approve the proposed rate adjustment, it will go into effect on January 1, 2022. The next fund review of the Solid Waste Utility will be presented to the Council in November or December 2022, unless there are significant changes in the fund (either positive or negative) by mid-year. If Council directs staff to shift the dates of the rate adjustments, the implementation of the rate adjustments and the timeline for the next fund review will be adjusted.

Staff will continue to closely monitor revenue returns for all utilities. In addition, staff will continue to review the operation of each utility to find opportunities to reduce expenditures.

Attachments

1. Resolution
2. Staff memo to the Utilities Commission (October 20, 2021)

RESOLUTION NO. 21-XXX, SERIES 2021

**RESOLUTION ENACTING MODIFICATION TO CITY OF DAVIS CUSTOMER RATES
FOR SOLID WASTE SERVICE FEES EFFECTIVE MARCH 1, 2019
TO IMPLEMENT FOURTH-YEAR RATE ADJUSTMENT ON JANUARY 1, 2022**

WHEREAS, Article 32.01.120 of the Davis Municipal Code authorizes the City Council to periodically amend, by resolution, fees for solid waste management services; and

WHEREAS, the City of Davis conducted a solid waste rate study, completed in October 2018 to review and recommend any necessary modifications to the City solid waste rates; and

WHEREAS, after a duly noticed public hearing on February 5, 2019, maximum solid waste service fees became effective March 1, 2019 with four additional maximum authorized annual increases thereafter through January 1, 2023; and

WHEREAS, these fees as established are for the purpose of maintaining and continuing the provision of the City's solid waste services; and

WHEREAS, the City Council retains the right to adjust or amend fees within the fee schedule established and adopted into the Municipal Code, and while the City Council has recognized that these are extraordinary times, the rate adjustments as established and approved through January 1, 2023 are necessary to ensure the fiscal resilience of the solid waste fund and prevent a future fund deficit.

NOW, THEREFORE, BE IT RESOLVED, by the City Council of the City of Davis that the fourth-year rate adjustment for the solid waste utility be implemented on January 1, 2022 at 5%.

PASSED AND ADOPTED by the City Council of the City of Davis on this 16th day of November, 2021, by the following vote:

AYES:

NOES:

Gloria Partida
Mayor

ATTEST:

Zoe S. Mirabile, CMC
City Clerk



Memorandum

Date: October 20, 2021
To: Utilities Commission
From: Stan Gryczko, Director, Public Works Utilities & Operations
Adrienne Heinig, Assistant to the Director
Subject: Item 7B – Solid Waste Annual Fund Review/Rate Adjustment
Recommendation to Council

Recommendation

1. Receive informational report on the status of the City's Solid Waste Fund (520); and
2. Approve staff recommendation to City Council that the fourth-year rate adjustment for the Solid Waste utility be implemented at 5%, with the adjustment occurring on January 1, 2022.

Background

Commission Discussion and Council Direction in October & December 2020

As part of the City Council direction to return each year with a report on the fiscal health of the Solid Waste fund, and a recommendation for the next year's rate adjustment (within the approved Proposition 218 period of rate adjustments), staff presented a fund update to the Utilities Commission on October 21, 2020, prior to the implementation of the planned 8% rate adjustment in January 2021. This adjustment discussion also included the consideration of the 10% rate adjustment postponed based on Commission recommendation and Council direction in May 2020. The June 2020 10% adjustment was postponed as a result of the COVID-19 pandemic and associated economic impacts. In addition to postponing the 10% adjustment in Solid Waste fees, the City Council also approved an urgency ordinance to in part waive new City utility bill late fees for all residential and commercial customers, allowing late payments without penalty through May 2020. This waiver was ultimately extended to April 2021.

Consideration of the Postponed Adjustment and Fund Performance during COVID-19

As stated in the report to the Commission in October 2020, until April 2020 the Solid Waste fund continued to perform at pace with expectations from the most recent cost of service study. While the fund expenditures did remain higher than revenue, and the fund balance continued to drop, the amount of the fund balance drop lessened by the

end of FY 19/20, as anticipated. This is consistent with the cost of service model showing a decrease in the fund balance until year 3 (2021) of the 5-year adjustment period, when revenue would overtake expenditures and the fund balance would begin to rebuild.

The impacts of a global pandemic, however, disrupted the return to health of the fund. From the report to Council on December 15, 2020 (Attachment 1):

“Staff have carefully tracked revenue from the utilities since March of this year, to identify any impacts of the actions by Council in March to forgo the implementation of new late fees for non-payment of utility bills, and note that the Solid Waste fund is the only utility fund that has seen appreciable impacts to revenue since the beginning of the COVID-19 pandemic response. Stormwater, Water and Wastewater utilities continue to see actual revenue each month at pace with previous year performance, or slightly higher.”

With revenue losses of \$40,000 on average each month, action was required to assure the health of the Fund, and to avoid incurring further debt. Staff recommended to the Commission in October 2020 that the rate adjustments consisting of 12% on January 1, 2021, and 6% on July 1, 2021 be implemented. This recommendation was supported by the Commission, with one dissent vote, and approved by Council.

June 2021 Fund Micro-Update

In the [Solid Waste Program Update, Senate Bill 1383 Implementation Planning and Other Current Topics](#) memo received by the Commission on June 16, 2021, staff included a short fund update focused on the Solid Waste fund balance. In June, the fund balance was anticipated to be lower than the fund balance calculated in October 2020, based on the reduction in rate revenue with commercial business closures during the shelter-in-place orders at the height of the COVID-19 pandemic.

Fund Update

The fund update presented in this report covers the City’s Solid Waste Fund (Fund No. 520) for Fiscal Year (FY) 2020-2021.

The revised Proposition 218 rate schedule:

Revised Prop 218 Rate Schedule (after 12/15/21 CC action)			
Mon/Year	Adjustment	\$ Impact	Rate (SFR 65 gal¹)
Mar 2019	13.5%	\$0.00	\$38.95
Jan 2021	12.0%	\$4.67	\$43.62
Jul 2021	6.0%	\$2.62	\$46.24
Jan 2022	5.0%	\$2.31	\$48.55

¹ The revised Prop 218 schedule included reflects dollar amount impacts presented with the average cart size per the Single-Family Rate (SFR)

Jan 2023	5.0%	\$2.43	\$50.98
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*Annual Commission Utility Fund Reviews - **Difference in Format for This Review***

This update is part of a regular series on the status of the City’s utility funds. The information presented includes a summary of the revenue and expenditures of the preceding closed fiscal year. The intent of the update is to give a snapshot of the status of the fund and highlight any outstanding differences between the actual data and the projected numbers from the model, in between full cost-of-service studies.

For the current fund review, there are two items of note for the Commission to consider. First, the implementation of Senate Bill (SB) 1383, and associated cost impacts, are not specifically included in the model being utilized for this current Proposition 218 schedule. Because of this, forecasting with the current model will likely not reflect the actual costs of the program moving forward. Second, the Commission will be considering a Request for Proposals (RFP) for a Solid Waste Cost of Service study to begin early next year, a study which will assess the probable cost increases associated with the implementation of SB 1383. For that reason, cash-in-hand balance, expenditures and revenues will not be projected past FY 2023.

Annual Fund Review

Sources of Funds

Solid Waste Fund revenues are collected from three sources: service charges paid by the utility customers, revenue from special drop box orders by customers, and interest paid from utility investments.

Service Charges

Service Charge revenue is the largest source of revenue for the Solid Waste Fund. In FY 2020-2021, the service charges for all customers totaled \$13,496,936.

Drop Boxes

Drop Box revenue is based on the number of drop boxes ordered and used in Davis, and is highly dependent on construction activity. In FY 2020-2021, the service charges totaled \$40,495.

Interest from Investments

Interest from investment revenue has historically been the smallest source of revenue for the Solid Waste Fund. In FY 2020-2021, the interest earned by the Solid Waste fund totaled \$27,280.

The most recent model developed for the fund was completed in 2019, and actual costs from FY 2017-2018 and city budget for FY 2018-2019 were used as the basis for the model’s projections. Model projections are used for comparisons of fiscal years after 2019.

When comparing the revenue included in the model (based on projections) to the actual revenue received in FY 2020-2021, there is a significant difference, as was expected given the impacts of the COVID-19 pandemic. While the actual revenue received by the City was higher than the budget predicted, the income was lower than anticipated in the model, likely due to the postponement of the June 2020 rate adjustment.

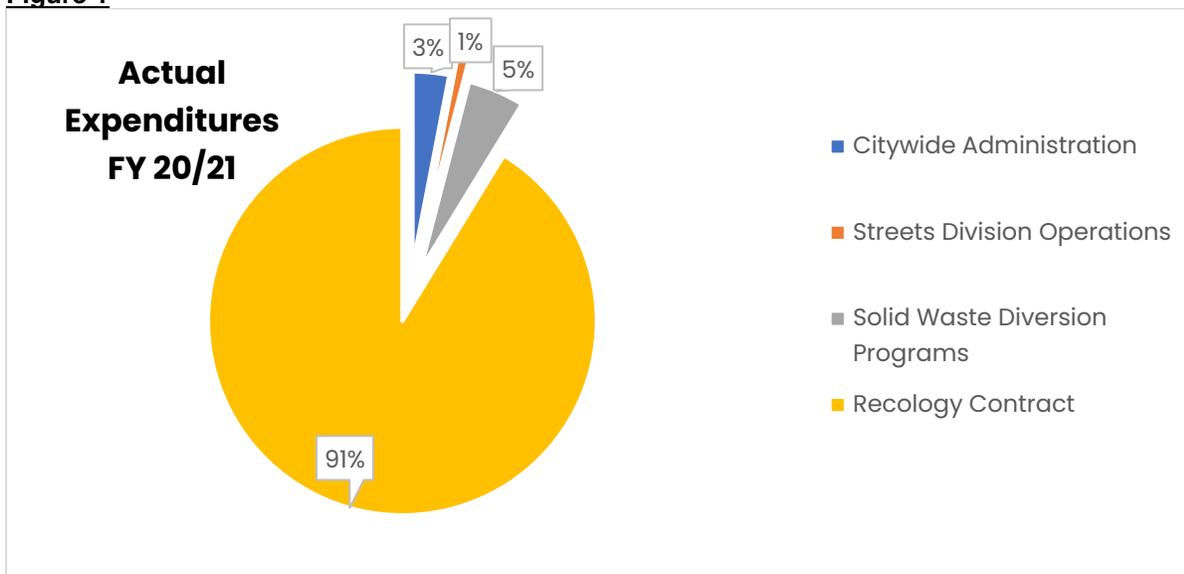
FY 2020-2021 Revenue	MODEL Forecast	BUDGET Projected	ACTUAL City Accounting
Service Charges	\$ 14,504,635	\$ 12,732,720	\$ 13,496,936
Other Revenues	\$ 40,000	\$ 66,142	\$ 40,495
Interest from Investments	\$ 0.00	\$ 0.00	\$ 27,280
Total Revenue	\$ 14,544,635	\$ 12,798,862	\$ 13,564,711

Within the fiscal year, rates were adjusted twice, in January 2021 (by 12%) and on July 1, 2021 (by 6%).

Uses of Funds

Expenditures for the utility are divided into four major sections: overall city administration, costs associated with Public Works Utilities and Operations hazardous waste removal, the City’s Solid Waste diversion programs, and the contract with the City’s solid waste hauler. A breakdown of costs using actual expenditure data is included in Figure 1 below.

Figure 1



City Administration

City administrative costs cover the operations and labor for work done in support of the Solid Waste Utility. This includes support for the Finance Division of the Administrative

Services Department, where the billing for the utility is done, the Fire Department, where hazardous waste removal is also performed, and for Public Works Utilities and Operations Department administrative staff outside of the Solid Waste Diversion programs. **Of note:** The City has been adjusting the budget and cost allocations over the last year. Due to this, there are changes in the budget from previous fiscal years, with new, revised or removed expenditure line items. Some Citywide overhead, for example, has been moved to a different expenditure line.

Streets Division

Streets Division costs include those incurred when performing hazardous waste and material clean up and disposal. The contract hauler costs associated with the City's street sweeping are also accounted for in the Streets program budget (in Figure 1 above, the street sweeping contract costs have been included with the waste hauling costs, to show the total cost of the Recology contract.)

Solid Waste Diversion Program

The second largest cost to the fund (though only 5% of the total), the Solid Waste Diversion program is the outreach, education, and regulatory side of the City's Solid Waste utility. This total also includes internal budget transfers and debt payments. Staff within the Diversion program are responsible for providing all outreach and education materials and tools for customers, from single-family residential customers through commercial customers, to ensure compliance with the City and State solid waste ordinances and requirements. Staff are also responsible for all reporting to regulatory bodies, including to CalRecycle, and coordinating the implementation of new regulations (such as Senate Bill 1383).

Contract Hauler

By far the largest component of the cost of the City's Solid Waste Utility, the contract hauler franchise agreement constitutes roughly 91% of the cost, and is currently held by Recology Davis. This includes the services to all City customers for waste hauling, the performance of annual waste audits, and the operation of the Materials Recovery Facility (MRF) in Davis, among other contractual obligations.

Discussion

With the changes (as previously discussed above) in the cost allocations across departments, the largest difference between the model, the budget and actual accounting is in expenditures.

The most significant differences are in the Solid Waste Diversion Programs, the Capital Improvement Projects, and the debt payment. All expenditures are summarized in the table below.

FY 2020-2021 Expenditures	MODEL Forecast	BUDGET Projected	ACTUAL City Accounting
Citywide Administration	\$ 594,800	\$ 659,305	\$ 402,695
Streets Division	\$ 93,700	\$ 107,417	\$ 82,529
Solid Waste Diversion Program	\$ 1,049,00	\$ 650,920	\$ 611,184
Capital Improvement Projects	\$ 362,000.00	\$ 15,000	\$ 0.00
Recology Contract	\$ 12,169,200	\$ 12,149,000	\$ 11,864,039
Debt Payment	\$ 233,500	\$ 60,600	\$ 0.00
Total Expenditures	\$13,453,200	\$13,642,242	\$12,960,447

The reductions in the Solid Waste Diversion program reflect the adjustments to cost allocations through the revision of the budget process over the last year. In FY 21/22, there is a restoration to a portion of these costs, and the budget reflects the trend of the last few fiscal years of program expenditures just over \$1M.

In the model, the contribution of funds to major upcoming projects (such as the environmental mitigation assessment of the old landfill site, and other projects discussed in 2019) are included in the calculations. With the revisions of the rate adjustments over the years, these projects have been pushed out to future years.

Similarly, the debt payments in the model include interest and principal. As discussed in the next section, the debt payments remain interest-only, based on the modifications to the rate adjustments over the years.

Debt

In May 2018 (FY 17/18), the Solid Waste Utility received a \$3,000,000 loan from the Wastewater Utility to maintain a positive fund balance and continue program operations in advance of the completion of the cost of service study, which had been delayed by about a year during the activity around the assigning of the City’s waste hauling contract to Recology Davis, after Recology purchased Davis Waste Removal (the former contractor).

The loan terms as originally prepared included a 10-year term, with interest-only payments required each year, and the full loan amount due by the end of the term. The initial recommendation from the consultant preparing the financial model for the Solid Waste utility included principal payments each year, in addition to the interest, to ensure timely payoff of the loan. However, this recommendation was accompanied by rate adjustments in March 2019 and each January thereafter until 2023. Council direction at

the February 5, 2019 meeting shifted the second-year increase to June 2020. This adoption reflected an adjustment to the loan payoff to 15 years, rather than 10 years. Subsequently, with postponement of the June 2020 rate adjustment, the model showed interest-only payments through the duration of the current Proposition 218 term, which will either result in a larger payment due at the end of the now 15-year term of the loan, or will necessitate an extension of the loan to 20 years, and higher payments of the principal than anticipated to offset the interest-only payments in FYs 2020, 2021 and 2022.

As of the writing of this report, the fund has paid a total of \$158,700 in interest toward the Wastewater Loan, with \$3,000,000 remaining in principal (note, this is a revision down from the previous report of \$186,900).

Reserve Calculations

The reserve calculation within the study, developed by the consultant working with the City in lieu of a formal reserve policy (which was in development at the time) was set at 15% of annual operating expenses for the utility. On January 28, 2020, the City Council adopted a formal reserve policy, which set the reserve calculation for the Solid Waste fund at 12 months of non-contractual operating expenses. When the costs associated with the Recology Davis contract are removed from the annual expenses, the remaining costs are roughly equivalent to 13% of annual operating costs, or about \$1.8 to \$2 million on average. With the postponement of the June 2020 adjustment to the fund, contributions to the development of the target reserve were decreased significantly.

Cash-in-Hand Balance/Fund Status

With the adjustments in cost allocations and expenditures, for this fund update we are not able to calculate the cash-in-hand balance (formally called fund balance). However, with the information available, there are positive notes to report. Fund expenditures appear to have dropped below revenue receipts for the first time since the beginning of the current Proposition 218 period, highlighting that the adjustments in revenue in January and July of this year aided the fund to meet the long-term goal. With the restored balance of the fund, the cash-in-hand balance should increase each year and ensure the development of the reserve fund balance. Additionally, ability of the fund to maintain cash-in-hand will be a significant benefit to the cost of service study next year, in assessing what impact the SB 1383 regulations will have on City ratepayers.

Upcoming 2021-2022 Budget

The request on hand is to review the current state of the Solid Waste Fund, and recommend a rate adjustment at or below the scheduled 5% adjustment on January 1, 2022. This report will also include some discussion of SB 1383, however the full costs of the regulations will likely take some time to take shape, as there are a number of discussions around process and policy (ultimately determined by City Council) that will need to be resolved before the full costs are known.

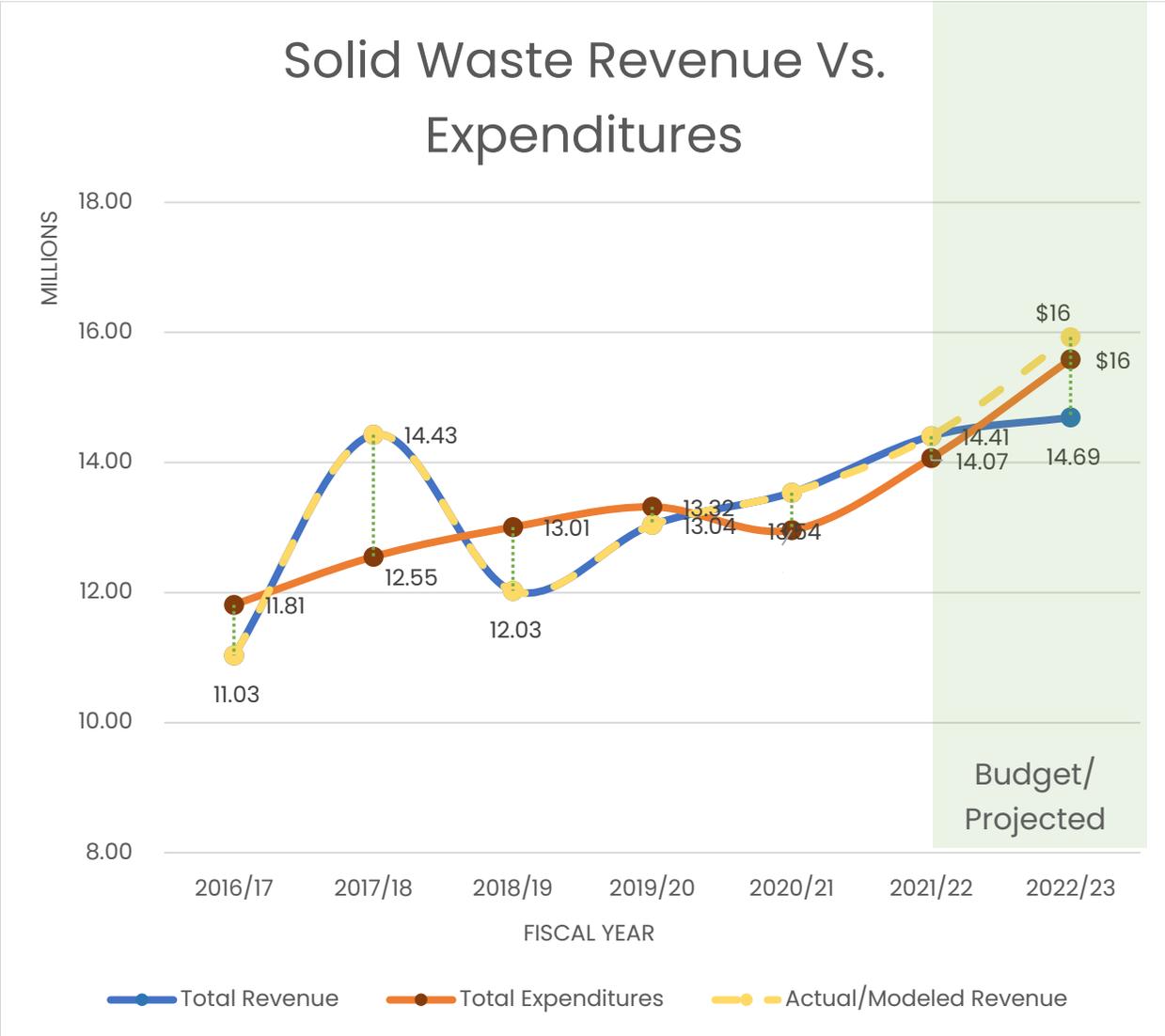
In 2020, and the beginning of 2021, the City's Solid Waste rate revenue was impacted by the COVID-19 pandemic, largely due to commercial customer account adjustments or closures, by roughly \$40,000 per month. However, the City did not see the anticipated scenario of a 10% reduction in revenue for the fiscal year as anticipated in October of 2020. Based on the revised model revenue developed by staff in October 2020 (to reflect the postponement of the June 2020 increase and reduced revenue from COVID-19), the forecast and budget for FY 2021-2022 are very similar. The table below reflects a 5% adjustment in rates for January 1, 2022.

FY 2021-2022 Revenue	MODEL Forecast	BUDGET Projected
Service Charges	\$ 14,506,323	\$ 14,366,300
Other Revenues	\$ 66,000	\$ 40,495
Interest from Investments	\$ 0.00	\$ 0.00
Total Revenue	\$ 14,572,323	\$ 14,406,795

The budget model with the January 1, 2022 adjustment of 5% shows that revenue is still on track to overtake expenditures within the next fiscal year (however just barely). The table below shows the modeled and budgeted expenditures for FY 2021-2022, and the chart shows the comparison of revenue to expenditures through 2022.

FY 2021-2022 Expenditures	MODEL Forecast	BUDGET Projected
Citywide Administration	\$ 613,000	\$ 364,509
Streets Division	\$ 96,800	\$ 83,822
Solid Waste Diversion Program	\$ 1,144,900	\$ 1,032,465
Capital Improvement Projects	\$ 362,000	\$ 0.00
Recology Contract	\$ 12,743,300	\$ 12,550,000
Debt Payment/Other Expenses	\$ 233,500	\$ 37,500
Total Expenditures	\$ 15,193,500	\$ 14,068,296

In a demonstration as to why the model is no longer useful to the projections on the Solid Waste Fund, the chart below shows the total revenue (blue solid line) and total expenditures (orange solid line) mapped over the last few fiscal years. The expenditures in the model for 2023 include the contribution of funds to major upcoming projects and the debt payments in the model include interest and principal, which accounts for the significant rise in expenditures in 2023. The revenue, adjusted for the impacts of 2020, is in blue, and the revenue included in the original model is shown in the yellow line.



What this chart demonstrates, in addition to the significant changes in the trajectory of the fund over the last year, is the precarious recovery of the balance of the fund, and the need to stay on track with that recovery, especially in light of the next cost of service study and the implementation of SB 1383.

Current Events

SB 1383

As of the drafting of the October 2020 fund update, the California Department of Resources, Recycling and Recovery (CalRecycle) had not finalized rulemaking on SB 1383 (Short-Lived Climate Pollutants: Organic Waste Methane Emissions Reductions), despite the implementation date of January 1, 2022. The rulemaking was finalized in November 2020, with the final language of the regulations released in February 2021.

With the release of the final regulations, City staff has been working with consultants, legal teams, internal working groups and County staff to develop implementation plans

for SB 1383 compliance both individually by jurisdiction, and collectively as a County (specifically for the development of the edible food recovery program). It should be noted that although the work towards SB 1383 compliance ramped up in early 2021 with the release of the final language, staff have been preparing for the regulations for a number of years.

As a reminder, SB 1383 establishes targets to achieve a 50 percent reduction in the level of the statewide disposal of organic waste from the 2014 level by 2020, and a 75 percent reduction by 2025. The law grants CalRecycle the regulatory authority required to achieve the organic waste disposal reduction targets and establishes an additional target that not less than 20 percent of currently disposed edible food is recovered for human consumption by 2025. The regulations will go into effect by into effect January 1, 2022, with the full implementation of the regulations in place by 2032.

There are a number of items in the regulations that would have impacts on Davis, and utility ratepayers, including the following:

- Changing the labels and lid colors for all Recology Davis collection bins to be complaint with the regulations (current bins do not match the requirements)
- The establishment of an edible food recovery program
- Translate a variety of mandated outreach items to customers in their native language (for any language spoken by 5% of more of our customers)
- New reporting requirements to the state
- City ordinance updates
- Inspections, audits and recordkeeping of organic waste generators, and more

The implementation of the city-wide mandatory organics collection program in 2016, along with the robust education and outreach program already in place, have put the City in an excellent place both in terms of meeting the requirements of the regulations, and already accounting for a significant cost in the rate structure.

City staff anticipates bringing the implementation roadmap developed with consultants to the Utilities Commission in November. The ordinance updates, along with the roadmap, will also be presented to the Natural Resources Commission, and staff will review the edible food recovery portion of the regulations with the Social Services Commission.

Solid Waste Rate Adjustment Staff Recommendation:

A rate adjustment of 5% on January 1, 2022

Month/Year	Adjustment	\$ Impact	Rate (SFR) 65 gal
Mar 2019	13.5%	\$0.00	\$38.95
Jan 2021	12%	\$4.67	\$43.62

Jul 2021	6%	\$2.62	\$46.24
Jan 2022	5%	\$2.31	\$48.55
Jul 2023	5%	\$2.43	\$50.93

The staff recommendation was developed with the following goals in mind; 1) to maintain the balance of the fund (with revenues exceeding expenditures), thus relieving the pressure on the fund balance, and 2) to allow for the continued development of the reserve, to provide a buffer against regulatory changes required in the next year. The current approved Proposition 218 rate schedule includes a 5% increase planned for January 1, 2022. With this recommendation, rate payers will see an increase of 5%, and the average single-family customer will pay \$2.31 more for solid waste services in 2022.

The recommendation from staff maintains the balance of the fund around the time originally anticipated, and brings the total fund balance up at a faster pace. With this adjustment, it is also likely that *future* rate adjustments (outside of the current Proposition 218 period) for the Solid Waste rates should be within previous expectations (around 5% annually), however the rate adjustments recommended might be higher to account for the regulatory changes and deferred payments to the loan or other deferred expenditures. As a reminder, the following assumptions have been made throughout the rate adjustments of this Proposition 218 schedule:

1. The full anticipated adjustment for the Proposition 218 approval period will be implemented. Scenarios which dropped a year of the adjustments demonstrated the action was not feasible to maintain the fund.
2. The scenarios assume that the next rate study would likely result in recommended rate adjustments slightly higher than anticipated with the original recommendations, and would be necessary to maintain the fund and to be able to implement projects and studies beyond basic utility operations.
3. For the remainder of the approved rate adjustment period, planned expenditures for any activities not immediately required for operations by the utility would be deferred indefinitely.
4. The target reserve would likely not be reached within the approved rate adjustment period, and the City would not have any cushion (fund balance above a reserve) to aid in rate impacts associated with the implementation of Senate Bill (SB) 1383. The fund would also not provide a cushion for additional regulatory changes, detailed rate reviews requested by the contract hauler, major emergencies, or other unforeseen financial impacts.

Rates of Surrounding Communities

In the review of Solid Waste rates in surrounding jurisdictions since October 2020, 6 of the 12 communities surveyed have raised rates. Likely this is in preparation for the implementation of SB 1383. Four of the jurisdictions surveyed (including the jurisdiction with the lowest solid waste rates) still do not have an organics program in place, and will likely see further rate increases in the short term to implement one. Also of note is the

provision of bi-weekly recycling services in Roseville, Elk Grove, Rancho Cordova and Sacramento, rather than weekly services as offered by Davis, in those jurisdictions with no organics program.

A summary of the jurisdictions surveyed and the basic services is included as Attachment 3. Please note, the table does not include detail related to program offerings such as free shred days, buy-back centers, bulky waste drop-off programs and other services that Davis residents receive free of charge.

Next Steps

The discussion and any recommendations from the Utilities Commission on rate adjustments for January 1, 2022 will be presented to Council in November or December (depending on the number of Utilities Commission meetings necessary to develop a recommendation).

As previously stated, the Commission will start the next cost of service/rate study in 2022, so fund updates for the Solid Waste Fund will be put on hold until the study is completed.

Attachments

1. City Council Meeting Item 03A - Solid Waste Fund Update and Rate Recommendation (December 15, 2020)
2. Fund Update Detail
3. Rates of Surrounding Jurisdictions