



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Rosalynn Hughey
Edgardo Garcia

SUBJECT: SEE BELOW

DATE: March 2, 2020

Approved

Date

3-4-20

SUBJECT: THIRD AMENDMENT TO CITY-GENERATED ZONE TOW SERVICES AGREEMENTS

RECOMMENDATION

- (a) Adopt a resolution authorizing the City Manager to negotiate and execute Third Amendments to the Agreements for City-Generated Zone Tow Services retroactive to January 1, 2020 through June 30, 2020 with one option to extend through the end of the contract term March 31, 2021 with the following tow operators (also known as SJ Towers):
- (1) Alongi Brothers, Inc. (San José, CA)
 - (2) Century Tow (San José, CA)
 - (3) City Towing, Inc. (San José, CA)
 - (4) Courtesy Tow Services, Inc. (San José, CA)
 - (5) Matos Auto Towing & Transport (San José, CA)
 - (6) Motor Body Company, Inc. (San José, CA)
- (b) The proposed amendment includes the following terms and conditions and revisions:
- (1) Reducing the contract compensation fee from \$59 to \$41;
 - (2) Modifying the definition of "Qualified Vehicles" and related list of qualified vehicle types eligible for reimbursement to include all vehicles types that otherwise meet the criteria for "Qualified Vehicles" under the contract; and
 - (3) Crediting the tow operators for operator expenses and lost profits related to disposing of *all* qualified vehicles that meet the defined criteria, against the proposed \$41 contract fee that is required to be remitted to the City.

OUTCOME

Approving the Third Amendment to the City-Generated Zone Tow Services Agreements will provide interim financial relief for the tow operators retroactively from January 1, 2020 through June 30, 2020 with the option to extend.

BACKGROUND

City-Generated Tow Services Audit and Council Direction

On January 15, 2019, the City Council accepted the City Auditor's "Audit of Towing Services: Changes to Contract Terms and Consolidated Oversight Could Improve Operations" Report and the Administration Response, and directed staff to return to the Transportation and Environment (T&E) Committee in fall 2019 with a proposed City-Generated Tow Services Delivery Model. Council also directed staff to consider various factors when developing the new model, such as accessibility for residents when determining tow zones and tow yard locations and an interim plan to address tow refusals. Additionally, as part of the March 2019 Council Priority Setting Session, Council green-lit the Council Priority Nomination to explore a "Temporary Municipal Recreational Vehicle and Trailer Specific Storage Facility" as part of the process to research and develop a new City-Generated Tow Services Delivery Model.

Tow Audit Work Plan and Tow Audit Working Group

Staff developed a comprehensive Tow Audit Work Plan outlining a near- and long-term strategy to accomplish the following goals:

1. Address all 17 tow audit recommendations
2. Develop a new City-generated tow service delivery model
3. Develop Request for Proposals (RFP) and recommend award of contract(s)
4. Transition the new program model from the Planning, Building and Code Enforcement Department to the Police Department by June 30, 2020

To achieve the work plan goals, staff formed the Tow Audit Working Group comprised of staff from multiple departments and offices including: Planning, Building and Code Enforcement, Police, Finance, Transportation, Civic Innovation, City Attorney, and City Manager. The Tow Audit Working Group met bi-weekly collaborating on interim improvement strategies, service model research through benchmarking, the release of two industry Request for Proposals (RFPs) to provide contingent tow services (back-up tows), and a Request for Information to generate information to inform the development of a new service delivery model framework.

Transportation and Environment Committee

On November 4, 2019, as directed by Council, staff presented the Status Report on the development of the new City-Generated Tow Services Delivery Model to the T&E Committee.¹ The Status Report included the Tow Audit Work Plan and Audit recommendation implementation progress to date. The Status Report also included the proposed new City-Generated Tow Services Delivery Model framework and pilot program including third-party administration, a full-service technology platform, a financially balanced and sustainable fee

¹ Transportation and Environment Committee City Generated Tow Services Status Report November 4, 2019

model, and modified contract terms and performance standards as appropriate. Staff identified three iterative phases for implementation of the pilot program: 1) financial analysis, 2) RFPs, and 3) contract amendments as appropriate with existing tow operators.

The T&E Committee accepted the Status Report and directed staff to:

- 1) Continue to refine the proposed service model and pilot program approach;
- 2) Explore an interim solution to provide financial relief to the six contracted tow operators, with a corresponding commitment to ensure responsive service; and
- 3) Return to T&E Committee in February 2020 with a final plan for implementation.

Following the November 4, 2019 T&E Committee, the Tow Audit Working Group worked to continue to refine the tow service delivery model and finalize the pilot program implementation plan. The Group also explored an interim solution to provide financial relief to the contracted tow operators for the remainder of the 2019-2020 fiscal year.

Staff conducted three follow up meetings with the current six tow operators (“SJ Towers”) on December 3, 2019, December 17, 2019, and January 15, 2020 to explore opportunities for interim financial relief. Additionally, the Tow Audit Working Group continued to meet bi-weekly to review and analyze all fees, costs, revenue, and budget (past and present), related to the City tow system to support staff’s recommendation for interim financial relief.

On February 3, 2020, staff returned to the T&E Committee with a status report including a proposed recommendation for interim financial relief as follows²:

Accept the recommendation for interim financial relief for tow operators from January 1 through June 30, 2020, with the option to extend, and return to City Council with:

- a. An amendment to the City Generated Tow Service Agreements retroactive to January 1, 2020 including:
 - i. Reducing the contract compensation fee from \$59 to \$41;
 - ii. Modify the definition of “Qualified Vehicles” and related list of qualified vehicle types eligible for reimbursement to include all vehicles types that otherwise meet the criteria for “Qualified Vehicles” under the contract; and
 - iii. Credit the tow operators for operator expenses and lost profits related to disposing of all qualified vehicles that meet the defined criteria, against the proposed \$41 contract fee that is required to be remitted to the City.

The T&E Committee approved staff’s recommendation and directed staff to return to Council with an amendment to the City Generated Tow Service Agreements to provide interim financial relief retroactively from January 1, 2020.

² Transportation and Environment Committee City Generated Tow Services Status Report February 3, 2020

ANALYSIS

SJ Towers have continued to express to the City their financial struggles and the need for financial relief from the current City-Generated Tow Services contract compensation fee. The Tow Audit Working Group held several meetings with SJ Towers to better understand their concerns, gather current financial data to verify their claims, and develop a proposal to provide interim financial relief to the operators that is fair, sustainable, and ensures continued City-generated tow service delivery.

Currently, the operators are contractually required to remit fees to the City monthly, including an \$8 fee per dispatch and a \$59 contract compensation fee per tow. To recoup some of the operating costs and lost profits, the operators can receive a credit for documented expenses and lost profits related to the disposal of qualified vehicles (such as recreational vehicles and trailers) to off-set the \$59 contract fee that is required to be remitted to the City until the remittance reaches zero.

Pursuant to the existing contract agreements, a "Qualified Vehicle" is currently limited to large vehicles that are eligible for up to \$100 credit for cleaning and \$226 credit for lost profit per vehicle. A "Qualified Vehicle" is defined as any recreational vehicle, motor home, camper, trailer, box truck, and various other types of defined large vehicles that 1) have not been claimed by the vehicle owner and do not generate revenue through the lien sale process, or 2) have been deemed scrap (valued at less than \$500) by the City upon issuance of a REG 462 form also known as a "junk-slip". This fee and credit system has been in effect since 2017 when Council directed staff to modify contract terms to reduce the contract compensation fee from \$80 to \$59 per tow and to add the qualified vehicle reimbursement option. In June 2019, Council directed staff to extend the modified contract compensation fee of \$59 per tow from July 1, 2019 until March 31, 2021, the end of the current contract term. The 2019-2020 Adopted Budget revenue estimate in the General Fund for these fees, after qualified vehicle credits, total \$360,000.

Despite the reduction in contract compensation fees charged to the tow operators and the establishment of the reimbursement structure since 2017, SJ Towers continue to express financial feasibility and labor intensity challenges. Community and industry challenges such as the increase in overall junk/low-value vehicle tows, the rising costs to tow and dispose of overall junk/low-value vehicles and the associated waste, and reductions in towed vehicles claimed by registered owners have continued to impact the operators "bottom line" and their ability to sustainably provide tow services. Based upon the information submitted by the operators to the City, the percentage of vehicles that are unclaimed by registered owners, are deemed junk, are disposed of, and scrapped is significant. In 2019, the tow operators reported that only 51% of towed vehicles were claimed, 49% went unclaimed, 11% were deemed junk vehicles, and 35% were disposed of or scrapped. Factors compounding their financial issues are: 1) the decline over the past few years of scrap metal prices, which reduces the revenue generated from salvaged vehicles; 2) the decline of revenues generated from lien sales; 3) and increased labor costs.

To review their claims, staff requested and used updated financial statements from SJ Towers to update the financial model that was used to determine the contract compensation fee reduction in 2017. This exercise indicated a further adjustment to the contract compensation fee is appropriate due to the factors mentioned above, which has had a limiting effect on revenue generated by City tow operators for City tow work, as well as the annual increases in the City's living wage has increased labor costs.

After completion of the financial review and further discussions with the operators, the Tow Audit Working Group concluded that reducing the contract compensation fee from \$59 to \$41 and expanding the definition of "Qualified Vehicles" to include all vehicles that 1) have not been claimed by the vehicle owner and do not generate revenue through the lien sale process, or 2) have been issued a REG 462 form ("junk-slip") by the City would provide the needed interim financial relief to the tow operators.

Therefore, staff recommends amending the current City-Generated Tow Services Agreements with the following terms and conditions, effective January 1, 2020 through June 30, 2020, with one option to extend to March 31, 2021, the end of the term of the existing agreements:

1. Decrease the contract fee that the operators remit to the City from \$59 per tow to \$41 per towed vehicle to offset increased labor and operational costs.
2. Expand the list of qualified vehicles to include any vehicle that 1) has not been claimed by the vehicle owner and do not generate revenue through the lien sale process, or 2) has been issued a REG 462 form ("junk-slip") by the City.
3. Credit the tow operators for operator expenses and lost profits related to disposing of qualified vehicles that meet the criteria, against the \$41 contract fee that is required to be remitted to the City.

EVALUATION AND FOLLOW-UP

If approved, the Third Amendment will be retroactive to January 1, 2020 through June 30, 2020 with one option to extend to the end of the contract term March 31, 2021. Staff will continue work to release an RFP for a technology/software platform and/or contract administration and return to Council in June 2020 with a recommendation for an award of the contract. Staff will bring forward proposed City-Generated Tow Services Delivery Model fees and charges, as appropriate, as part of the 2020-2021 Proposed Budget process to support the new City-Generated Tow Services Delivery Program, software, and/or contract administration.

CLIMATE SMART SAN JOSE

The recommendation in this memo has no effect on Climate Smart San José energy, water, or mobility goals.

PUBLIC/STAKEHOLDER OUTREACH

Staff conducted three follow-up meetings with SJ Towers to gain an understanding of the need for financial relief and obtain financial information to support the recommended interim relief.

COORDINATION

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

COMMISSION RECOMMENDATION/INPUT

This item does not have input from a board or commission.

FISCAL/POLICY ALIGNMENT

This action is consistent with the City's 2019-2020 Operating Budget City Service Areas Delivery Framework for Performance-Driven Government for Operational Services.

COST SUMMARY/IMPLICATIONS

The 2019-2020 Adopted Budget includes a revenue estimate of \$360,000 from City-Generated Tow Service fees, which includes the contract compensation fee minus the credit for junk vehicles. Reducing the tow services contract compensation fee from \$59 to \$41 would result in a reduction of \$18 per tow for tows conducted over the remainder of the fiscal year, retroactive to January 1, 2020. Additionally, expanding the definition of "Qualified vehicles" from large low-value vehicles, such as recreational vehicles and trailers, to include any vehicle that cannot be lien sold for revenue or is deemed junk by the City may result in increased credits to the tow operators further reducing the projected revenue. Staff anticipates a potential budgetary impact, in the General Fund, between \$200,000 to \$250,000 as a result of the recommended actions in this memorandum. If necessary, recommended budget actions to recognize the loss in revenues, offset by higher than budgeted collections in other revenue categories, may be brought forward for City Council approval as part of the 2019-2020 Year-End Budget process.

HONORABLE MAYOR AND CITY COUNCIL

March 2, 2020

Subject: Third Amendment to City Generated Tow Service Agreements

Page 7

Staff will continue to research and evaluate the costs, fees, and budget needed to support a financially balanced and sustainable new City-Generated Tow Service Delivery Model. Staff notes these items will need to be worked through and finalized as part of the tow software and/or contract administration RFP process and award of contract to a third-party, pending negotiations and contract agreement amendments with SJ Towers, and ultimately within the 2020-2021 Proposed Budget process.

CEQA

Not a Project, Public Project Number PP17-003, Agreements/Contracts (New or Amended) resulting in no physical changes to the environment.

/s/

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San Jose Police Department

/s/

ROSALYNN HUGHEY, Director
Planning, Building, and Code Enforcement

For questions, please contact Rachel Roberts, Deputy Director of Code Enforcement, at (408) 535-7719.