



# Memorandum

**TO:** HONORABLE MAYOR  
AND CITY COUNCIL

**FROM:** Kerrie Romanow

**SUBJECT:** SEE BELOW

**DATE:** February 10, 2021

Approved

Date

02/12/21

**SUBJECT: PRELIMINARY FORECAST ON RESIDENTIAL GARBAGE AND RECYCLING RATES**

## **RECOMMENDATION**

Accept the report on potential 2021-2022 customer rate increases for residential garbage and recycling services that are anticipated to be proposed to the City Council in June 2021.

## **OUTCOME**

This update provides information on the forecasted 2021-2022 customer rate increases for residential garbage and recycling services, currently estimated to be:

- Twenty-one percent for Single-Family Dwelling (SFD) households (an increase of \$8.21 per month or \$1.89 per week for the typical service level), and
- Seven percent for Multi-Family Dwelling (MFD) households (an increase of approximately \$1.61 per month or \$0.37 per week per dwelling unit).

While these projected rate increases are necessary to maintain cost-recovery, given the unprecedented challenges and economic impacts caused by the COVID-19 pandemic, the City is continuing to pursue additional options for ratepayer cost reductions in an effort to reduce estimated rate increases for 2021-2022 as much as possible without altering service delivery, which is in more demand than ever by residents given stay-at-home orders. This report reviews the reasons for the cost increases and the potential strategies that staff will pursue in an attempt to achieve lower levels of rate increases.

With the City reducing last year's planned customer rate increases with several unconventional, one-time financial offsets (such as planning to sell a property), it will be even more challenging to reduce projected rate increases this year without impacting service delivery.

## **BACKGROUND**

Residential garbage and recycling rates are set to cover the expenses of providing services to all households in the City. Staff regularly reviews Integrated Waste Management (IWM) Fund revenues and expenditures and forecasts the rates necessary to implement and maintain Council-approved services, programs, and activities related to residential garbage and recycling services.

Before the COVID-19 pandemic, modifications to residential garbage and recycling services and the associated contractual cost increases were approved by City Council to improve customer service and keep services running beyond the contractual expiration date of June 30, 2021. In accordance with this decision, future rate increases were strategized to accommodate the new pricing and program parameters to keep services at cost-recovery. Given the unprecedented and difficult times caused by the pandemic, the Environmental Services Department (ESD), in collaboration with the City Manager's Budget Office, implemented unconventional, near-term measures to offset a portion of the rate increases planned for 2020-2021. These measures included: ESD freezing vacant staff positions, withdrawing a proposal for additional staffing support for program enforcement, planning to sell property, and ensuring that any savings from 2019-2020 was available to help offset rate. These actions were estimated to generate a net savings of \$6.02 million.

In addition, the Administration asked the residential garbage and recycling contractors to consider cost reduction measures for 2020-2021 to help mitigate rate increases during this challenging time for San José residents, and all four contractors gave a one percent waiver to the 2020-2021 cost-of-living adjustment, which totaled a one-time savings of \$1.15 million.

Together, the City's unconventional measures and the contractors' compensation waiver reduced the SFD customer rate increase by six percent (from fifteen percent to nine percent) and the MFD customer rate increase by two percent (from seven percent to five percent).<sup>1</sup> However, as the actions to achieve net cost savings in 2020-2021 were one-time in nature, the memorandum recommending the revised rates also indicated that the cost of service delivery in 2021-2022 would require significant rate increases of approximately 20%.

## **ANALYSIS**

Residential garbage and recycling services include: garbage, recycling and yard trimming collection; recycling processing; yard trimmings processing and composting; junk pickup; SFD motor oil and oil filter on-demand collection; and processing of residential garbage to recover organics and recyclables. Contractors collect half a million tons of material every year, from over 320,000 households, while providing garbage and recycling processing services that give San José one of the highest recycling rates in the country.

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<sup>1</sup> <https://sanjose.legistar.com/View.ashx?M=F&ID=8595037&GUID=8BF2CC29-E902-413E-A7E4-06F330DB64E9>

During the COVID-19 pandemic, as typical day-to-day life has been disrupted and uncertainty has prevailed, residential garbage and recycling contractors have continued to provide reliable, essential services to residents. As residents have stayed at home, the contractors have handled over ten percent more material compared to before the pandemic and have processed more contaminated recyclables, while taking a one percent compensation reduction in 2020-2021 to help offset a portion of the customer rate increases.

To maintain reliable services for our community, residential garbage and recycling contractors quickly adapted to the difficult conditions with operational adjustments, new safety protocols and equipment, and timely communication and coordination with the City. The contractors have persisted while these novel challenges come at an already difficult time for the recycling industry as traditional recycling markets can no longer be counted on, and markets that currently exist demand higher quality material, requiring recycling companies to invest more in processing operations.

Some helpful trends for the contractors during the pandemic have been an increase in recyclables sold (e.g., cardboard boxes from on-line orders) and less traffic on the roads, making for more efficient collection operations.

### ***Increasing Contractual Costs and Impacts from Stay-at-Home Orders***

The projected proposed rate increases are needed to cover increasing contractual costs from new pricing going into effect and impacts from the COVID-19 pandemic stay-at-home orders.

Primary reasons for these cost increases include:

- New pricing for extended services – To continue residential garbage and recycling services beyond June 30, 2021, Council approved pricing and terms in 2019 to extend services with all current contractors through June 30, 2036 and authorized the City Manager to negotiate and execute the contract extensions. Terms of this extension include customer service enhancements, compliance commitments with new State law, and variable pricing for recycling services that correlate with the level of contamination of recyclables collected.
- Recycling contamination – In fall 2020, a contractually required bi-annual third-party expert study of recyclables collected indicates an increase of ten to twenty percent in recycling contamination as residents seem to be using their recycling containers for garbage to deal with the increased volume of garbage generated during stay-at-home orders. Following the terms of the extended services, this study will be used to set the pricing level for recycling contractors, which means higher contamination of the recyclables collected results in higher payments to the recycling contractors for the next two fiscal years.
- Junk Pickup – this service continues to see record-level participation by residents, especially during stay-at-home orders when large items collected have more than doubled.

- Annual inflationary (“cost of living”) adjustments for contractors – The City’s agreements with the residential garbage and recycling contractors provide for annual inflationary adjustments in compensation. This is a standard provision for solid waste agreements, especially necessary given the expenses, including labor, to operate in the Bay Area.

***Current and Projected Rates in the Local Marketplace***

SFD and MFD garbage and recycling customer rates of regional cities are shown in the tables below. Services included with these rates vary from city to city, and San José’s services are generally more robust, including unlimited recycling, unlimited loose in the street yard trimmings collection (with optional cart subscription), unlimited on-demand junk pickups at no additional cost, used oil collection, and processing of all waste to recover organics and recyclables. This combination of services results in San José having one of the most effective residential recycling programs in the area.

SFD Garbage and Recycling Program 32-Gallon Rate Comparison

<b>Regional Jurisdictions</b>	<b>FY 20-21 Monthly Rate</b>
San Francisco	\$52.59
Oakland	\$51.27
Palo Alto	\$50.07
<b>San José (Forecasted)</b>	<b>\$47.33</b>
Santa Clara	\$44.10
Fremont	\$39.74
<b>San José (Current)</b>	<b>\$39.12</b>
Sunnyvale	\$37.36
Hayward	\$35.62

Under the current forecasted proposed increases, an SFD increase of twenty-one percent to the 32-gallon garbage cart (used by 90 percent of SFD customers) would result in a monthly increase of \$8.21, from \$39.12 to \$47.33. Excluding rate increases for 2021-2022 from other jurisdictions that are not yet known but anticipated in the near-term, especially with implementation of State regulations related to Senate Bill 1383, this projected 2021-2022 monthly rate would still be lower than other highly populated cities in the area.

MFD Garbage and Recycling Program 3-Cubic Yard Bin Rate Comparison

	<b>Monthly Rate</b>
Countywide Average	\$334.85
<b>San José (Current)</b>	<b>\$267.62</b>

An MFD increase of seven percent to the 3-cubic yard bin serviced once per week (one of the most common service levels) would result in a monthly increase of \$18.73, from \$267.62 to \$286.35, an approximate increase of \$1.61 per month per dwelling unit. The projected proposed MFD rate remains twenty percent lower than the 2019-2020 County-wide average rate of \$334.85.

### ***Exploring Reductions to Projected Rate Increases***

City staff will continue to pursue additional options for ratepayer cost reductions to reduce proposed rate increases for 2021-2022 as much as possible. As more financial and program information becomes available over the next couple months, City staff will fine tune projected costs and revenues, and explore administrative cost saving measures; however these efforts are not anticipated to reduce the planned rate increases by more than a couple percentage points.

For example, while contractual expenses make up the vast majority (90 percent) of program costs, ESD will explore ways to reduce internal costs. The City's staff and support for residential garbage and recycling services continues to be at approximately ten percent of overall program costs, which is on the lower end of the typical proportion for contracted garbage and recycling services. To keep overhead cost lower than projected, ESD plans to continue to freeze staff positions funded by residential garbage and recycling ratepayers.

ESD will also continue to further explore potential alternate funding options, beyond those already used in the IWM Fund to lessen the impact of the 2020-2021 rate increases, including the potential spending from the Operations and Maintenance Reserve and the potential allocation of future emergency relief funding.

As an essential service, it is critical to ensure that the IWM Fund remains sufficiently resourced, even in the case of extreme emergencies. For this reason, the IWM Fund maintains an Operations and Maintenance Reserve of \$14.0 million in 2020-2021 as a backstop against any revenue collection problem or sudden surges in emergency costs. This reserve is equal to approximately one month of operating costs. Though an unusual step that would not normally be recommended, the City could consider a very small drawdown of this reserve in 2021-2022 to help pay for a portion of the anticipated cost increases. This would again be a one-time solution – and would require additional rate increases in the future to replenish the reserve – but it is a potential bridging strategy for consideration as the community begins its economic recovery. It is important to note that the IWM Fund previously had a rate stabilization reserve that was liquidated to offset rate increases in 2019-2020, so the City's ability to rely on one-time reserves to offset ongoing expenditure needs while still ensuring the overall stability of this essential operation is very limited.

During the pandemic, some cities have used Federal relief funds to help offset increased costs of residential garbage and recycling services caused by stay-at-home orders. While the City of San José has been very targeted in the use of its emergency relief funding to assist our most vulnerable, should any eligible future relief funding become available, approximately \$10

million dollars of forecasted cost increases for garbage and recycling services in 2021-2022 are tied to stay-at-home orders (e.g., increased recycling contamination, increased garbage generation, and increased participation in Junk Pickup service), and that could potentially be considered to be covered by the relief funds, if eligible. Any recommendation to allocate relief funding to help offset rate increases would first require City Council discussion and approval. On-going cost reductions that would mitigate the projected rate increases now and in the future by more than a percentage point would likely require substantial modifications and reductions to the current services offered to residents. An example of such a modification would be altering the currently unlimited SFD Junk Pickup service so that residents are limited to a certain amount of Junk Pickup appointments per year, such as two 3-item pickups per year. While such a modification would reduce costs for garbage and recycling services, it could have detrimental impacts by causing residents to pay more to dispose of items beyond the limit imposed on the Junk Pickup service. Residents continue to participate in this service at record-setting levels, with a more than 400% increase in collections compared to the previous service model. Customer satisfaction surveys indicate this service is highly rated by residents as it provides a convenient way to dispose of large items, and this aligns with the City's efforts to reduce blight and beautify the City. Even more drastic alternatives would include the modification of the agreements with Recycle Plus haulers to eliminate back-end processing for SFD customers and transfer garbage collection to landfill instead of processing to recover organics and recyclables. While this could yield significant rate reduction, it would also be a significant step backward in achieving waste reduction and climate goals and would jeopardize the City's significant progress towards SB 1383 implementation, which requires organics be diverted from landfill.

Potential options for reducing forecasted rate increases are summarized in the table below.

Potential Option	Estimated Percentage Point Reduction to Forecasted Rate Increases	Concerns
Keep freezes on staff vacancies from last year’s rate reductions (Environmental Inspector, Environmental Services Specialist)	SFD: Less than 1% MFD: Less than 1%	<ul style="list-style-type: none"> <li>• Staff support needed to implement new solid waste requirements from the State (SB 1383) and address recycling contamination</li> <li>• One-time offset, would likely make future rate increases higher than planned</li> </ul>
Limit currently unlimited SFD Junk Pickup to two 3-item pickups per year	SFD: 2-3%	<ul style="list-style-type: none"> <li>• Popular, highly rated service with residents, collections increased by over 400% compared to previous service model</li> </ul>
Modify the agreement with Recycle Plus haulers to reduce back-end processing for SFD customers and transfer garbage collection to landfill instead of processing to recover organics and recyclables	SFD: 4-6%	<ul style="list-style-type: none"> <li>• Decreases single-family residential landfill diversion from 80% to 50%</li> <li>• Not compliant with City goals</li> <li>• Inconsistent with State waste regulations as directed by SB 1383 that requires a 75% reduction of organic waste disposal</li> </ul>
Other funding sources, such as partial use of Operations and Maintenance Reserve, and identification of future emergency relief funds	TBD	<ul style="list-style-type: none"> <li>• Any use of reserve funding makes the fund less resilient should an emergency situation arise</li> <li>• Potential upcoming Federal relief funds are unknown and there are competing priorities for these funds</li> <li>• One-time offset, would likely make future rate increases higher than planned</li> </ul>

**CONCLUSION**

At this early stage of the budget development cycle, projected rate increases for 2021-2022 of \$8.21 per month for the typical service level for SFD services and approximately \$1.61 per month per dwelling unit for MFD services would maintain the program at near cost-recovery, meet contractual obligations, and continue the current level of services for residents.

Given the unprecedented challenges and economic impacts caused by the COVID-19 pandemic, the City is continuing to pursue several options for ratepayer cost reductions to reduce proposed rate increases for 2021-2022 as much as possible.

**EVALUATION AND FOLLOW-UP**

As rate increase offsets are explored, and as more financial and program information becomes available in the next couple months, IWM Fund revenues and expenses will be adjusted correspondingly before the Proposed Operating Budget and the proposed customer rate increases are brought forward for Council’s consideration in May 2021 and June 2021 respectively.

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### **CLIMATE SMART SAN JOSE**

The recommendation in this memo aligns with one or more Climate Smart San José energy, water, or mobility goals.

### **PUBLIC OUTREACH**

As required under California law, notices for proposed maximum rate increase for 2021-2022 will be mailed to property owners that are subject to these rates in spring 2021. After the notices are mailed, there will be a public protest period prior to the Council meeting when rate increases will be considered by Council.

This memo will be posted on the City's website for the Council Agenda of February 23, 2021.

### **COORDINATION**

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

### **COMMISSION RECOMMENDATION/INPUT**

There is no commission recommendation/input associated with this action.

### **FISCAL/POLICY ALIGNMENT**

The projected additional revenue generated by the projected rate increases aligns with City Council Policy that programs be self-supporting whenever possible.

### **COST SUMMARY/IMPLICATIONS**

There are no cost implications at this time. The 2021-2022 Proposed Operating Budget (IWM Fund Statement of Source and Use of Funds) and the proposed customer rate increases for residential garbage and recycling services will be brought forward for Council's consideration later this fiscal year.



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**CEQA**

Not a Project, File No. PP17-009, Staff Reports, Assessments, Annual Reports, and Informational Memos that involve no approvals of any City action.

/s/

KERRIE ROMANOW

Director, Environmental Services

For questions, please contact Valerie Osmond, Deputy Director, Environmental Service Department, at (408) 535-8557.