



# ADMINISTRATION AND FINANCE



## STAFF REPORT

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To: SBWMA Board Members  
From: Hilary Gans, Interim Executive Director & Facility Operations Contract Manager  
Date: July 28, 2016 Board of Directors Meeting  
Subject: Resolution Approving Shoreway Tip Fee Increase

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### Recommendation

It is recommended that the SBWMA Board of Directors approve Resolution No. 2016-29 attached hereto authorizing the following action:

**Increase the Franchise and Non-Franchise Tip Fee at Shoreway by \$10.00 per Ton for FY16/17.**

### Summary

The FY16/17 Budget approved by the Board in June 2016 proposed a Shoreway tip fee increase for franchise and non-franchise customers of \$10.00 per ton. At the June Board meeting, there was further discussion about the amount of the tip fees increase. Specifically, there was discussion about lowering the franchise tip fee from the recommended \$10 per ton to \$9.00 per ton for franchise tonnage and to amend the Budget if necessary. The two points raised in support of lowering the franchise tip fee were as follows:

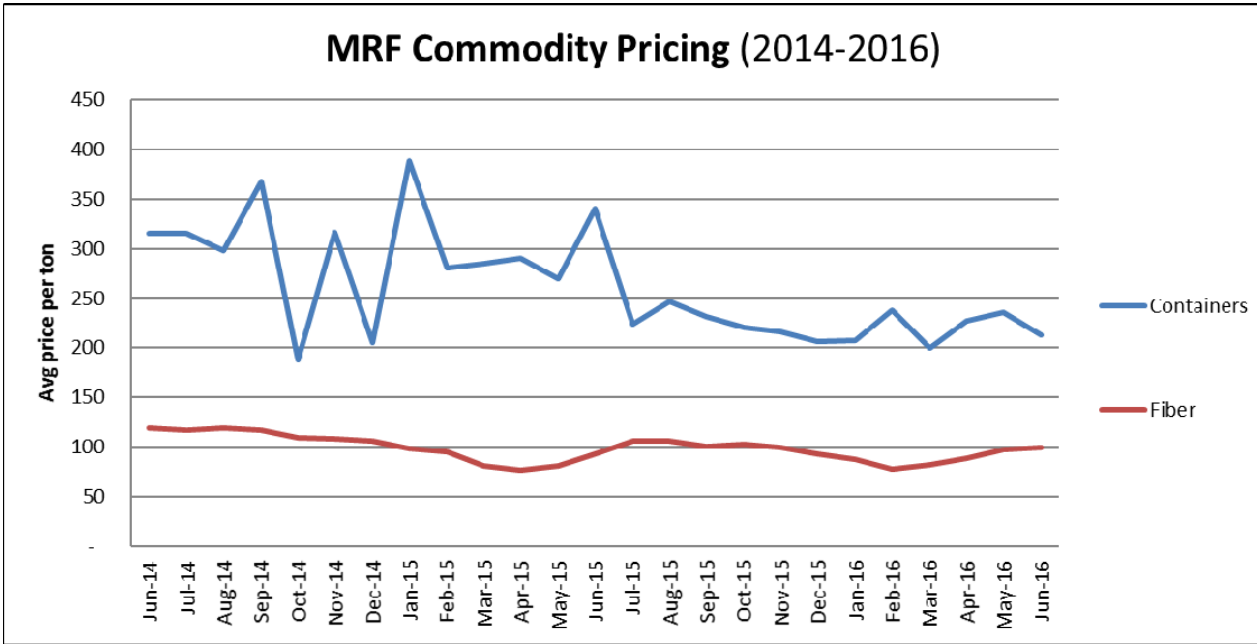
1. If commodity values have improved since the FY16/17 Budget was prepared in March, should franchise tip fees be lowered to reflect an updated commodity market forecast?
2. Can non-franchise tip fees be raised more than budgeted so that franchise tip fees can be less than \$10 per ton?

### Analysis of FY16/17 Budgeted Tip Fees

The FY16/17 Budget recommended a tip fee increase of \$10 per ton for franchise and non-franchise/self-haul tonnage delivered to Shoreway. The dollar amount of the proposed tip fee increase was based on the budget goals of: 1) creating a balanced operating budget, 2) maintaining Reserves balances, and 3) replacing a gap in revenue resulting from lower commodity revenues. The proposed \$10 per ton across-the-board tip fee increase in the FY16/17 Budget forecasts meets these goals by 1) providing a near-breakeven Operating Budget with an end of year Cash Flow projection of -\$267,232 on a total budget amount of \$44,667,519, 2) maintaining an Undesignated Reserve balance of \$2,968,453, and 3) replaces the revenue loss from declining commodity prices.

### Budgeted Commodity Revenue Forecast

When the FY16/17 Budget was prepared and first presented to the Board in March, commodity markets were at the bottom of a two-year price decline. Since March, commodity prices seem to have stabilized and have shown slight signs of recovery. At the June Board meeting, there was a discussion and a request to update the budget forecast using recent commodity prices and analyze the impact of the commodity revenue updated on the FY16/17 Budget.



As illustrated in the graph above (MRF Commodity Pricing), commodity prices have shown signs of recovery in the second quarter of 2016 (For example, the price per ton for containers averaged \$225 in Q2 vs. \$215 in Q1 and the price per ton for fiber averaged \$100 in Q2 vs. \$83 in Q1). If the favorable commodity pricing trend continues over the next 12 months, the SBWMA could expect an increase in commodity revenues over what was forecast in the FY16/17 Budget. As shown in Table 1, staff forecasts that there could be a positive revenue variance of \$413,154 for FY16/17 over what was forecasted in the Budget report.

Commodity Type	Tons/Year	Original Budget	Update From	Variance
		March-16	June-16	
		Price /ton	Price /ton	
<b>Containers</b>	18,145	\$226.65	\$213.32	\$ (13.33)
<b>Fiber</b>	53,190	\$82.59	\$94.91	\$ 12.31
<b>Annual Forecasted Commodity Revenue</b>		\$ 8,505,782	\$ 8,918,936	\$ 413,154

Since commodity sales revenues help offset Shoreway operating expenses, the improved commodity revenue forecast would result in improved Net Cash Flow. Specifically, the FY16/17 Budget projected an end of year Net Cash Flow of -\$267,232 (see FY16/17 Budget report, Table 1-Summary). An updated budget forecast based on June's commodity pricing would revise the estimated Net Cash Flow to positive \$145,922 for the fiscal year.

To relate updated commodity forecast to its impact on the franchise tip fee structure, staff has calculated that a franchise tip fee reduction of -\$1.00 per ton would result in a loss of revenue of -\$284,206 on a calendar year basis (note that the tip fee increase on franchise tonnage becomes effective January 1, 2017 and therefore impacts only 6 months of the budgeted annual revenues). As shown in Table 2, the variance from the commodity update and tip fee reduction would result in a forecasted end-of-year FY16/17 Net Income of -\$128,948.

Net Income from FY16/17 Budget	(\$267,232)
Variance from Commodity Update	\$145,922
Variance from Tip Fee Reduction	(\$284,206)
Updated FY16/17 Net Income	(\$405,516)

***Effect of Non-Franchise Tip Fee Adjustments on the Budget***

When the FY16/17 Budget was prepared, staff assigned the same \$10.00 per ton tip fee increase on all tonnage entering Shoreway without distinction between franchise and non-franchise customers. The non-franchise tip fee increase was scheduled in two phases so to minimize “rate-shock” to the self-haul customers and reduce the risk of customers leaving Shoreway for other disposal locations (the first installment was made on July 1<sup>st</sup> with a \$5.00 per ton increase and a second \$5.00 per ton tip fee increases is scheduled for January 2017).

At the June Board meeting there was discussion about shifting more of the tip fee rate increase onto non-franchise customer with the goal of reducing the burden on franchise customers. Specifically, there was a recommendation of lowering the franchise tip fee \$1.00 per ton (from \$10 to \$9). In the sections below, Staff has analyzed several aspects of the non-franchise tonnage in an attempt to provide information to the Board Members about non-franchise tip fee adjustment options.

Non-Franchise Revenues Contribution to the Budget

As shown in **Table 5**, non-franchise tip fee revenues account for \$8.11M of the \$36.50M budgeted Total Tip Fee Revenues - Non-Franchise tip fees contribute 22% while Franchise tip fees contribute 78% of the total Tip Fee Revenues. *(note table is unchanged from the original Budget staff report).*

Revenues	FY15/16 Adopted Budget	FY15/16 Mid-Year Projections	FY16/17 Preliminary Budget	Variance	Variance %
Tip Fee Revenues	\$33,602,300	\$34,171,148	\$36,508,044	\$2,905,744	9%
Non Franchised	6,982,300	7,434,730	8,114,936	1,132,636	16%
Franchised	26,620,000	26,736,417	28,393,108	1,773,108	7%
Net Commodity Sales Revenues*	7,668,100	6,999,627	6,943,411	(724,689)	-9%
MRF - Host Fees	443,500	400,000	403,070	(40,430)	-9%
Interest Income	48,200	54,508	78,940	30,740	64%
HHW and Other Revenue	761,800	757,800	734,054	(27,746)	-4%
<b>Total Revenues:</b>	<b>\$42,523,900</b>	<b>\$42,383,083</b>	<b>\$44,667,519</b>	<b>\$2,143,619</b>	<b>5%</b>

*\*Gross commodity sales – 28% revenue share with SBR and buyback payments.*

Non-Franchise Tip Fees Are Set to Cover Costs

The tip fees charged non-franchise/self-haul customers are set at a level equal to the cost of handling materials at Shoreway and disposing of the materials. While there is no positive cash flow benefit to the SBWMA from non-franchise tonnage, the incremental revenues from non-franchise tip fees does contribute to defraying some of Shoreway’s fixed costs. Staff analyzed the benefit of the non-franchise revenues and estimates that \$897,200 or 10% of the non-franchise tip fee revenue is applied to fixed costs of Shoreway. If there is a change in non-franchise tip fee revenues, (resulting from an increase or decrease in tip fee or in tonnage delivered to Shoreway), franchise tip fees would require a corresponding adjustment.

Balancing Franchise and Non-Franchise Revenues

Shoreway tip fee revenue is comprised of 22% non-franchise revenue and 78% franchise revenue (Table 5). Therefore, a decrease of \$1.00 in franchise tip fee would require a corresponding increase of ~\$5.00 in non-franchise tip fees to balance-out revenues. This would require raising the non-franchise tip fee \$15 on self-haul customers instead of the planned \$10 per ton. In preparing the FY16/17 Budget, staff anticipated that the \$10 per ton tip fee increase will result in a 20% loss in self-haul customer tonnage. If the non-franchise tip fee is increased an additional \$5.00 there would likely be a larger self-haul customer defection rate as customers could choose to drive to local competitor facilities (Ox Mtn Landfill or Zanker located roughly 15 miles from Shoreway).

Budget Impact of a Revenue Surplus or Deficit

FY16/17 budgeted Net Income is tied to the Undesignated Reserve account: at the end of FY16/17 the Net Income position of the Agency will impact the Undesignated Reserve by increasing or decreasing the Undesignated Reserve balance. As presented in the Budget staff report, the Undesignated Reserve functions as a savings account for the Agency and in the past the Undesignated Reserve account balance has been used to cover imbalances between expenses and revenues. **Table 3** shows the historic and proposed FY16/17 Undesignated Reserve balances and the relationship to tip fee adjustments (*table is unchanged from the original budget staff report*).

Table 3. Undesignated Reserve Trend and Tip Fee Adjustments (Past 3 budget years)				
	FY13/14 Actual	FY14/15 Actual	FY15/16 Adopted	FY16/17 Proposed
Undesignated Reserve Balance	\$ 5,952,546	\$ 5,023,699	\$ 3,175,018	\$ 2,968,453
Net Change in Reserves	\$ -	\$ (928,847)	\$ (1,848,681)	\$ (206,565)
Approved tip fee increase	3.2% tip fee increase	No tip fee increase	2% tip fee increase	10% (\$10.00) tip fee increase
Collection Rate Impact of tip fee change	Unreported	0.00%	0.60%	2.80%
Reason for change in net income	Unreported	Expenses exceed revenues	Expenses exceed revenues, Comm. price drop midyear	Low commodity prices forecasted

***Non-Franchise Tonnage vs. "Third-Party Recyclables"***

To clarify a point discussed at the June Board meeting, Third-Party Recyclables are a category of materials that are separate from Non-Franchise materials. The term "Third-Party Recyclables" is used to refer to single-stream recyclable materials delivered to the Shoreway MRF by other Recology operations outside of the SBWMA. The third-party recyclables are delivered under an agreement between SBR and Recology (the SBWMA is not a party to the agreement). SBR and the SBWMA have a separate agreement that establishes the payment of a "Host Fee" that SBR pays to the SBWMA for the privilege of using the Shoreway MRF. The budgeted host fee revenues forecast for FY16/17 are \$403,070 (Table 5). The host fee revenues are used by the Agency to offset facility operating expenses and thereby reduce tip fees.

***Tip Fee Increase Effect on Residential Collection Rates***

The FY16/17 Budget forecasts an average residential collection rate increase of \$0.93 per month for a 32 gallon garbage can (see **Table 4** *unchanged from original budget staff report*). Staff calculated that a franchise tip fee increase of \$9 vs. \$10 per ton would the effect of lowering Member Agency's collection rates, roughly \$0.10 (from the budget forecasted amount of \$0.93 to \$0.84 per month).

<b>Table 4. Estimated Franchise Collection Rate Impact</b>		
<i>Based on \$10.00 Shoreway Tip Fee Increase (effective 1/1/17)</i>		
<b>2016 Collection Rate Impact</b>	<b>% Increase *</b>	<b>Resi. Rate Impact (32 gal.) Cost/Mo.</b>
Atherton	3.1%	\$ 1.72
Belmont	2.3%	\$ 0.81
Burlingame	2.8%	\$ 0.67
East Palo Alto <sup>1</sup>	3.5%	\$ 1.44
Foster City	2.8%	\$ 0.61
Hillsborough	2.3%	\$ 1.19
Menlo Park	2.8%	\$ 0.66
N. Fair Oaks	3.2%	\$ 0.87
Redwood City	3.0%	\$ 0.81
San Carlos	2.5%	\$ 0.79
City San Mateo	2.7%	\$ 0.58
West Bay Sanitary	2.7%	\$ 1.00
County San Mateo (CFA)	2.6%	\$ 0.92
<b>TOTAL SBWMA AVERAGE</b>	<b>2.8%</b>	<b>\$0.93</b>
<sup>1</sup> All residential accounts receive a 96-gallon garbage cart.		
* The rate increase % is for total collection revenue. Member Agencies decide how to allocate the actual rate increase across residential and commercial account service levels.		

**Background**

The SBWMA FY16/17 Budget was presented to the Board in April, in May, and was approved at the June Board meeting. In the June budget discussion there was interest by Board Members to analyze the tip fee structure and the proposed FY16/17 Budget tip fee increase of \$10.00 per ton.

**Fiscal Impact**

The FY16/17 Budget staff report forecasted an annual Net Income for FY16/17 of -\$267,232. Adjusting the Shoreway tip fees will have fiscal impacts and alter the assumptions in the FY16/17 Budget.

**Attachments:**

Resolution 2016-29



## RESOLUTION NO. 2016-29

### RESOLUTION OF THE SOUTH BAYSIDE WASTE MANAGEMENT AUTHORITY BOARD OF DIRECTORS TO INCREASE THE FRANCHISE AND NON-FRANCHISE TIP FEE AT SHOREWAY BY \$10.00 PER TON

**WHEREAS**, the SBWMA is responsible for setting the Shoreway Tip Fees for Franchise and Non-Franchise tonnage to meet the Revenue Requirements of the Agency,

**WHEREAS**, the FY16/17 Budget was approved by the Board of Directors on June 23<sup>rd</sup>, 2016 and a tip fee increase of \$10 per ton was included in the budget revenue projections,

**NOW, THEREFORE BE IT RESOLVED** that the South Bayside Waste Management Authority hereby approves a FY16/17 Franchise tip fee increase of \$10 per ton to be effective January 1<sup>st</sup>, 2017 and a Non-Franchise tip fee increase of \$5.00 per ton effective July 1<sup>st</sup>, 2016 and a \$5.00 per ton increase effective January 1<sup>st</sup>, 2017.

**PASSED AND ADOPTED** by the Board of Directors of the South Bayside Waste Management Authority, County of San Mateo, State of California on the 28<sup>th</sup> day of July, 2016, by the following vote:

Agency	Yes	No	Abstain	Absent	Agency	Yes	No	Abstain	Absent
Atherton					Menlo Park				
Belmont					Redwood City				
Burlingame					San Carlos				
East Palo Alto					San Mateo				
Foster City					County of San Mateo				
Hillsborough					West Bay Sanitary Dist				

I HEREBY CERTIFY that the foregoing Resolution No. 2016-29 was duly and regularly adopted at a regular meeting of the South Bayside Waste Management Authority on July 28, 2016.

ATTEST:

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Bob Grassilli, Chairperson of SBWMA

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Cyndi Urman, Board Secretary



## STAFF REPORT

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To: SBWMA Board Members  
From: Cliff Feldman, Recycling Programs Manager  
Hilary Gans, Shoreway Facility Manager  
Date: July 28, 2016 Board of Directors Meeting  
Subject: Resolution Approving Findings from Review of Collection Services and Facility Operations Reports, Tonnage Data and Customer Service Systems Audits for 2015

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### Recommendation

It is recommended that the SBWMA Board of Directors approve Resolution No. 2016-30 attached hereto authorizing the following action:

**Approve the Findings from Review of Collection Services and Facility Operations Reports, Tonnage Data and Customer Service Systems Audits for calendar year 2015.**

### Summary

The Agreements with Recology SBR prescribe standards for reporting and operating performance. The information collected and reported to the SBWMA by the contractors is substantially self-reported (e.g., all Shoreway tonnage data and the collection route and call center performance). To ensure the integrity of the reported data, the SBWMA conducts an annual third-party audit. The auditing work reveals how well both Recology and SBR obtained, compiled and reported data to the SBWMA and Member Agencies. R3 conducted the audit and prepared a report of Recology's and SBR's performance for 2015 (see Exhibit A). Overall, the audit found that both companies are in substantial compliance with requirements of the Agreements audited and it recommended only minor financial and operational corrections.

### Analysis

In April 2016, R3 Consulting (R3) commenced the annual auditing project to conduct a Review of Collection Services and Facility Operations reports, tonnage data and customer service systems audits that covered the calendar year 2015; and concluded with submittal of a final report in June 2016. The goal of the audit is to review the largely self-reported financial and operational information provided by the contractors to ensure the accuracy of the information and to make sure proper management controls are in place. While the SBWMA conducts this audit annually, the scope of work varies somewhat depending upon the follow up items from the previous year's audit findings and as staff adjusts the audit scope to address areas of concern.

R3 identified several areas where both Recology and SBR were found to be compliant and non-compliant with the operational and reporting requirements of the Franchise and Facility Operations Agreements for calendar year 2015. The results of this auditing work are summarized in the Recommendations Section of the report (see Section 9 in **Exhibit A - Review of Collection Services and Facility Operations Reports, Tonnage Data and Customer Service Systems Audits for Calendar Year 2015**).



## Recology

The primary emphasis of the auditing work was related to assessment of the information provided in *Recology's Annual Report for 2015* issued to the Member Agencies on February 15, 2016. The auditing focused on:

- tons collected,
- customer service data, and
- calculation of liquidated damages and performance incentive/disincentive payments.

The Recology Franchise Agreement(s) are structured to place a high priority on customer service and diversion program performance and include performance standards and incentives for high performance (meeting or not meeting these standards has financial implications to both the Member Agencies and Recology). Specifically, Recology can earn incentive payments through annual diversion from landfill achieved, and if certain customer service and operational performance standards are not met, then Recology must pay liquidated damages.

The information used to determine compliance with the performance standards and the performance standards are measured from the customer service call center data compiled and self-reported by Recology. The audit revealed the company under reported the number of complaints collection quality, including: missed pick up initial complaints, improper placement of containers, excessive noise and unacceptable employee behavior. Table 1 below summarizes the corrections that should be made to Recology's Annual Report. The adjustments to payments to/from the Member Agencies will be captured in the revised *Recology's 2017 Application for an Adjustment to Contractor's Compensation* due to the Member Agencies and SBWMA on July 22, 2016.

Table 1

<b>Adjustment of Liquidated Damages and Performance Incentives/Disincentives Paid to the Member Agencies</b>	
<b>Performance Standard</b>	<b>Owed to Member Agencies</b>
Unacceptable Employee Behavior	\$1,462
Missed Pick Up Collection Events*	-\$50
Unauthorized Collection Hours and Property Damage Complaints	\$809
Vehicle Fluid Spills	\$875
	\$3,096
*Negative value denotes overpayment by Recology.	

Recology is provided an allowance that must be exceeded before being deemed non-compliant for some performance standards (e.g., unauthorized collection hours, improper placement of containers, excessive noise complaints), for others there is zero tolerance (e.g., unacceptable employee behavior, missed pick-ups, vehicle fluid spills). As customer calls and complaints are received by Recology, these calls are given a "Reason Code," which then necessitates a variety of follow-up measures. Recology ultimately uses the Reason Code data to report on its compliance with the various performance standards and resultant Liquidated Damages payments to the Member Agencies and the Performance Incentive/Disincentive payments to/from the Member Agencies). While Recology has made improvements implementing recommendations from the annual operational audit process, there are still issues related to Recology not consistently coding and reporting customer inquiries and complaints. As a result, the R3 audit report includes recommendations for Recology to improve call handling. Staff has worked with Recology to develop the prior and current recommendations, which the company has agreed to implement.

### ***South Bay Recycling (SBR)***

Tonnage, material category, and tip fee payment information recorded by the scales by SBR serves as the "base-data" for all of Recology's and SBR's waste handling functions (e.g., tonnage for all vehicles entering and leaving the Shoreway facility is recorded by SBR and provided to Recology's for use in the Annual Report for 2015 that is issued to the Member Agencies). It is therefore critical that accurate information be collected, recorded, and reported by SBR. The SBWMA staff review the tonnage information reported by SBR on a monthly basis and verify its accuracy. The audit serves as an important third-party check on the data and data management performed by SBR and the R3 audit of SBR's operations relates specifically to assessing the accuracy of tonnage information recording at the scales and ensuring that reported tonnage data is used consistently by SBR and Recology. The scope of the annual operational audit includes the following components:

- Verify Accuracy of SBR's reported In-Bound Tonnage Data
- Verify SBR's reported data (from franchised services) is consistent with Recology's reports
- Verify all other SBR tonnage is also accurate
  - o Franchised Inbound Tons (Recology)
  - o Member Agency Vehicles Inbound Tons
  - o Recology Maintenance Box Trucks
  - o Self-Haul Tons
  - o Buyback & Drop-Off Tons
  - o South Bay Internal Tons
  - o Non-Franchised Tons

The audit did not find any material inaccuracies in SBR's reporting for 2015 and therefore no recommendations for follow up by SBR are included in the R3 report.

An additional audit task performed by R3 included the verification of contractual requirements that are tied to Liquidated Damages. Specifically, R3 verified SBR's procedures to identify and report events which would trigger Liquidated Damages and then verified that Liquidated Damages payments were properly calculated and tie to the reported events. The audit did not find any instances of non-compliance by SBR and no material recommendations were made by in the report.

### **Background**

The Collection Services Franchise Agreements with Recology and the Facility Operations Agreement with SBR prescribe standards for reporting and operating performance. The information contained in the contractor's reports is substantially self-reported by both companies (e.g., all tonnage data from the Shoreway scales and the collection route and call center performance data as well as the collection Liquidated Damage events identified in attachment J of the Franchise Agreements. To ensure the integrity of the data reported by Recology and SBR, the SBWMA conducts a third-party audit of the data managed and reported by both companies (the audit included assessing Recology's call center functions to ensure the accuracy of transcribing and reporting information, complaints and requests for service from customers. The scope of auditing SBR's operations was limited to the scale house operations (i.e., tonnage reporting) and reporting of commodity revenues). The auditing work reveals how well both Recology and SBR obtained, compiled and reported data to the Member Agencies per the requirements prescribed in the Franchise Agreement(s) and Shoreway Facility Operations Agreement, respectively.

### **Fiscal Impact**

The cost for R3 to conduct this audit was \$34,816 for FY15/16. The audit fiscal impact results in revisions to the Liquidated Damages and Performance Disincentive payments calculated by Recology in its 2015 Annual

Report. The audit results in increased Liquidated Damages and Performance Disincentive payments owed by Recology to the Member Agencies totaling \$3,096 (the will be credited to the Member Agencies in the Recology 2016 Compensation Application for calendar year 2017). Prior years audit expense are as follows: \$36,159 for FY14/15, \$46,000 for FY13/14 and the audits resulted in payments by Recology of \$8,426 for calendar year 2014 and \$16,650 for calendar year 2013).

**Attachments:**

Resolution 2016-30

[Exhibit A - R3 Report: Collection Services and Facility Operations Reports, Systems, Tonnage, Data and Customer Service Systems Auditing Project for 2015](#) (Available online only at [www.rethinkwaste.org](http://www.rethinkwaste.org))



## RESOLUTION NO. 2016-30

### RESOLUTION OF THE SOUTH BAYSIDE WASTE MANAGEMENT AUTHORITY BOARD OF DIRECTORS APPROVING THE FINDINGS FROM REVIEW OF COLLECTION SERVICES AND FACILITY OPERATIONS REPORTS, TONNAGE DATA AND CUSTOMER SERVICE SYSTEM AUDITS FOR 2015

**WHEREAS**, the South Bayside Waste Management Authority (SBWMA) Board of Directors has authorized an annual audit of Recology San Mateo County and South Bay Recycling:

**WHEREAS**, at the February 25, 2016 SBWMA Board of Directors meeting, the Board approved Resolution Number 2016-12 authorizing staff to contract with R3 Consultants to perform the audit of Recology and SBR for calendar year 2015; and,

**WHEREAS**, the audit results found in Exhibit A increase Liquidated Damages and Performance Disincentives payments due to the Member Agencies from Recology totaling \$3,096,

**NOW, THEREFORE BE IT RESOLVED** that the South Bayside Waste Management Authority hereby approves the Findings from Review of Collection Services and Facility Operations Reports, Tonnage Data and Customer Service Systems Audits for calendar year 2015.

**PASSED AND ADOPTED** by the Board of Directors of the South Bayside Waste Management Authority, County of San Mateo, State of California on the 28<sup>th</sup> day of July, 2016, by the following vote:

Agency	Yes	No	Abstain	Absent	Agency	Yes	No	Abstain	Absent
Atherton					Menlo Park				
Belmont					Redwood City				
Burlingame					San Carlos				
East Palo Alto					San Mateo				
Foster City					County of San Mateo				
Hillsborough					West Bay Sanitary District				

I HEREBY CERTIFY that the foregoing Resolution No. 2016-30 was duly and regularly adopted at a regular meeting of the South Bayside Waste Management Authority on July 28, 2016.

ATTEST:

\_\_\_\_\_  
Bob Grassilli, Chairperson of SBWMA

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Cyndi Urman, Board Secretary



A Public Agency

## STAFF REPORT

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**To:** SBWMA Board Members  
**From:** Farouk Fakira, Finance Manager  
**Date:** July 28, 2016 Board of Director's Meeting  
**Subject:** Resolution Approving Findings from 2015 Financial and Accounting Systems Audit of Recology and SBR

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### Recommendation

It is recommended that the SBWMA Board of Directors approve Resolution No. 2016-31 attached hereto authorizing the following action:

**Approve the Report on the 2015 Financial and Accounting Systems Audit of Recology and SBR**

### Summary

On an annual basis, the SBWMA hires a third-party auditor to review significant financial transactions and the financial systems of Recology and SBR to ensure the integrity of the financial information from the contractors. R3 Consultants have completed an audit of year 2015 and have provided the agency with a Report (See Exhibit A). The Audit Report indicate that no substantial financial errors were found with either contractor's financial reports and payments. By approving this Resolution, the Board is also approving the revenue reconciliation balances that are owed to/from Recology to each Member Agency: shown in **Table 1**. (Note that these approved balances will be incorporated into the annual Revenue Requirement figures to be considered for approval by the Board at the September 22, 2016 Board meeting).

### Analysis

The financial audit work performed by R3 Consulting covering calendar year 2015 (The work commenced in April 2016 and concluded with submittal of the final audit report titled "R3 Financial Systems Audit of 2015 Collection Services and Facility Operations Contractors Report" (see **Exhibit A**). This audit work is an important part of our fiduciary responsibilities to our Member Agencies as it relates to monitoring contractor financial compliance with their respective agreements (i.e., Member Agency Franchise Agreement and Shoreway Operations Agreement). An important part of this audit process is to verify that all information from the contractor's is properly reported by Member Agency. While errors in allocation of financial data between Member Agencies would have no impact on Recology, it could have a big impact on individual agencies.

R3 reviewed the reporting of financial data and payments to the SBWMA and our Member Agencies by Recology and SBR as applicable and the Audit Report makes separate recommendations for Recology and SBR. Specifically, there was ~\$100 million of rate payer's gross billings that flowed through Recology's financial reporting system and another ~\$17 million was paid by SBR to the SBWMA for recycling commodities and gate revenue collected from public customers using the Shoreway Environmental Center.

### *Recology*

For Recology, the primary focus of the audit is the 2015 Revenue Reconciliation which is submitted by Recology on March 31 each year for the prior calendar year. This report reconciles the amount paid to Recology from customer billings (less the payments to Member Agencies for franchise fees and to the SBWMA for tip fees at the Shoreway

Environmental Center) compared to the Board approved compensation owed to Recology for providing collection services by the Member Agencies. The result is a surplus or shortfall owed to/from Recology by Member Agency. In total, the 2015 surplus is \$121,886 which is less than 1% of gross revenue as shown in **Table 1**.

**Table 1**

2015 Revenue RECONCILIATION FINAL	RECOLOGY BILLING	RECOLOGY PAYMENTS & ADJUSTMENTS				NET AMOUN "PAID" TO RECOLOGY	AMOUNT OWED TO RECOLOGY	BALANCE DUE (TO)/FROM RECOLOGY
Service Area	Revenue Billed	Less: Expenses Disposal/ Processing	Agency Fees	"Extra" Services by Recology	Other, 2013 Balance	Subtotal Revenue less Expenses	Recology Base Services	FINAL Surplus/ (Shortfall)
Atherton	\$ 3,188,740	\$ (936,889)	\$ (334,074)	\$ (32,077)	\$ (145,437)	\$ 1,740,263	\$ 1,461,074	\$ 279,189
Belmont	6,558,771	(1,377,409)	(1,629,298)	(68,608)	(940,070)	2,543,386	3,620,978	(1,077,592)
Burlingame	10,690,190	(3,114,083)	(1,790,549)	(102,721)	41,259	5,724,096	5,729,318	(5,222)
East Palo Alto	4,594,914	(1,492,457)	(781,018)	(49,392)	134,974	2,407,021	2,410,949	(3,928)
Foster City	5,778,606	(1,453,745)	(412,566)	(22,262)	(333,499)	3,556,534	3,466,353	90,181
Hillsborough	3,151,168	(718,197)	(303,128)	(13,388)	356,908	2,473,363	1,967,587	505,776
Menlo Park	10,321,736	(2,752,608)	(1,707,583)	(134,731)	(160,011)	5,566,803	5,838,582	(271,779)
North Fair Oaks	2,695,770	(774,828)	(142,617)	(35,560)	17,634	1,760,399	1,770,658	(10,259)
Redwood City	18,466,567	(5,055,914)	(2,635,148)	(141,917)	144,629	10,778,217	10,561,173	217,044
San Carlos	8,228,769	(1,887,223)	(953,958)	(98,767)	(97,186)	5,191,635	5,090,254	101,381
San Mateo	21,929,464	(5,467,271)	(2,960,056)	(355,012)	(433,685)	12,713,440	12,662,789	50,651
West Bay	1,504,471	(388,516)	(82,588)	(16,972)	15,717	1,032,112	996,526	35,586
County	3,199,374	(760,360)	(179,181)	(19,146)	117,433	2,358,120	2,147,262	210,858
<b>SBWMA Total</b>	<b>\$ 100,308,540</b>	<b>\$ (26,179,500)</b>	<b>\$ (13,911,764)</b>	<b>\$ (1,090,553)</b>	<b>\$ (1,281,334)</b>	<b>\$ 57,845,389</b>	<b>\$ 57,723,503</b>	<b>\$ 121,886</b>
%	100%	26%	14%	1%	1%	58%	58%	0%

The Audit of Recology's Revenue Reconciliation Report found that "The balances reported by Recology in their Revenue Reconciliation report are verified as accurate". Note that the Shoreway tip fee expense is a pass-through expense for Recology between the Member Agencies and the SBWMA and this has no impact on Recology's Revenue Reconciliation. The 2015 Revenue Reconciliation from Recology is found in **Attachment A**.

Regarding the account balances between Recology and the Member Agencies, eight Member Agencies have a 2015 surplus balance with Recology and can be reimbursed from Recology (as noted in the MOU, Section E.3 (see **Attachment B**), Agencies with surplus balances can request by July 31, 2016, a refund from Recology of the surplus balance). Since these funds belong to the rate payers and not to the Member Agency so care must be taken to keep these funds separate from the Member Agency general fund. If a refund is not requested, the balance will be retained by Recology and credited towards future Agency balances (all balances held by Recology are "owned" by the rate payers and not Recology). All balances (surplus or shortfall) will be part of the draft Total Revenue Requirement reported by the SBWMA to the Member Agencies on August 12, 2016 in the *Draft Report Reviewing Recology's 2017 Compensation Application*.

**Table 2** below compares the final 2015 surplus/shortfall balance to what was estimated in the 2016 Total Rate Report issued by the SBWMA in September 2015 and the ending balances for most Member Agencies are close to the SBWMA's projections with the following notable variances;

- Negative variances were due to lower billed revenue and were experienced in Burlingame, Menlo Park, and Redwood City.
- Negative variances due to slightly higher disposal tonnage were experienced in Burlingame and Menlo Park.
- And, positive variance due to lower franchise fees was experienced in Burlingame.

(The 2015 estimate is from the September 24, 2015 Board package, 6A staff report on the 2016 Recology Compensation Application, Exhibit A, Table 8.)

**Table 2**

2015 SURPLUS/ (SHORTFALL)	ESTIMATE @ Sept. 2015	Final @ June 2016	Variance
Member Agency:			<i>Better/(Worse)</i>
Atherton	\$ 277,572	279,189	\$ 1,617
Belmont	(1,260,543)	(1,077,592)	182,951
Burlingame	140,417	(5,222)	(145,639)
East Palo Alto	(65,403)	(3,928)	61,475
Foster City	31,623	90,181	58,558
Hillsborough	501,837	505,776	3,939
Menlo Park	(137,597)	(271,779)	(134,182)
North Fair Oaks	(29,735)	(10,259)	19,476
Redwood City	326,799	217,044	(109,755)
San Carlos	50,887	101,381	50,494
San Mateo	24,310	50,651	26,341
West Bay	31,409	35,586	4,177
County	197,757	210,858	13,101
<b>SBWMA Total</b>	<b>\$ 89,333</b>	<b>\$ 121,886</b>	<b>\$ 32,553</b>
			36%

**SBR**

For SBR, the financial audit report verified that payments made by SBR to the SBWMA for public revenue and gross commodity revenue were accurate. In addition, the audit reviewed the scale house procedures and has made recommendations on various improvements.

**Background**

The information and data contained in both contractors' reports are substantially self-reported by the companies and the annual audit performed by a third-party consultant serves a critical function of helping to ensure the accuracy of financial transactions. The general purpose of the audit was to perform an evaluation and verification of financial reporting systems, processes and record keeping, analysis and audit of billing and revenue, and analyze and audit the allocation of revenue and costs to the twelve Member Agencies.

The Agreements with Recology prescribe numerous reporting and payment requirements including paying franchise fees to the Member Agencies and payments to the SBWMA of tipping fees at the Shoreway facility for disposal and processing expenses. Recology also must track collected tonnage by material type and by Member Agency, allocate disposal cost to Member Agencies and prepare an annual revenue reconciliation report showing the net surplus/shortfall owed to/from Recology by each Member Agency. This project also entailed a review of Recology 2015 Annual Revenue Reconciliation, Attachment Q revenue and costs, and customer billing rates.

The Shoreway Facility Operations Agreement with SBR requires the company to pay to the SBWMA all commodity revenue (from the sale of commodities) and public gate revenue. The SBR review included a verification of public revenue and commodity revenue reported and paid to the SBWMA for 2015. Tonnage reporting and commodity prices are reviewed.

### **Fiscal Impact**

The cost of the Financial Audit work performed by R3 under this contract was \$35,743 on a budget amount of \$40,000. The actual cost is lower due to negotiating a lower cost proposal from R3 than last year's audit cost.

### **Attachments:**

[Exhibit A - R3 Financial Systems Audit of 2015 Collection Services and Facility Operations Contractors Report](#) (Available online only at [www.rethinkwaste.org](http://www.rethinkwaste.org))

Attachment A – Recology Revenue Reconciliation (3/31/2016)

Attachment B – MOU with Recology on Interest Calculation on Surplus/Shortfall Balances





## RESOLUTION NO. 2016-31

### RESOLUTION OF THE SOUTH BAYSIDE WASTE MANAGEMENT AUTHORITY BOARD OF DIRECTORS APPROVING FINDINGS FROM 2015 FINANCIAL AND ACCOUNTING SYSTEMS AUDIT OF RECOLOGY AND SBR

**WHEREAS**, the South Bayside Waste Management Authority Board of Directors previously approved the need for an annual Financial Systems audit of our contractors – Recology and SBR, and

**WHEREAS**, the South Bayside Waste Management Authority Board of Directors approved the selection of R3 Consultants to perform the audit, and

**WHEREAS**, R3 has submitted their audit report to the SBWMA staff, and

**WHEREAS**, the SBWMA staff has reviewed the audit report and recommends the South Bayside Waste Management Authority Board of Directors to approve the audit report and the recommendations in Attachment A.

**NOW, THEREFORE BE IT RESOLVED** that the South Bayside Waste Management Authority hereby approves the Financial Systems audit report prepared by R3 and agrees to their recommendations.

**PASSED AND ADOPTED** by the Board of Directors of the South Bayside Waste Management Authority, County of San Mateo, State of California on the 28<sup>th</sup> day of July, 2016, by the following vote:

Agency	Yes	No	Abstain	Absent	Agency	Yes	No	Abstain	Absent
Atherton					Menlo Park				
Belmont					Redwood City				
Burlingame					San Carlos				
East Palo Alto					San Mateo				
Foster City					County of San Mateo				
Hillsborough					West Bay Sanitary Dist.				

I HEREBY CERTIFY that the foregoing Resolution No. 2016-31 was duly and regularly adopted at a regular meeting of the South Bayside Waste Management Authority on July 28, 2016.

ATTEST:

\_\_\_\_\_  
Bill Widmer, Chairperson of SBWMA

\_\_\_\_\_  
Cyndi Urman, Board Secretary



March 31, 2016

Hilary Gans  
Interim Executive Director  
SBWMA/RethinkWaste  
610 Elm Street, Suite 202  
San Carlos, CA 94070

Dear Mr. Gans:

Enclosed is a copy of the Revenue Reconciliation Rate Year 2015 in accordance with Attachment K, Section 8 of the Agreement. Recology will send electronic copies to each jurisdiction.

If you should have any questions or require additional information, please call me at (650) 598-8243.

Sincerely,

A handwritten signature in blue ink that reads 'Mario Puccinelli'.

Mario Puccinelli  
General Manager  
Recology San Mateo County

cc: Cliff Feldman  
Farouk Fakira



# **RECOLOGY SAN MATEO COUNTY**

## **REVENUE RECONCILIATION RATE YEAR 2015**

**Submitted  
MARCH 31, 2016**



## **REVENUE RECONCILIATION RATE YEAR 2015**

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Recology San Mateo County  
 Revenue Reconciliation  
 Rate Year 2015  
 Revenue Reconciliation of Gross Revenue  
 Billed to Approved Contractor's Compensation  
 and Surplus/Shortfall

	<u>Atherton</u>	<u>Belmont</u>	<u>Burlingame</u>	<u>E Palo Alto</u>	<u>Foster City</u>	<u>Hillsborough</u>	<u>Menlo Park</u>	<u>North Fair Oaks</u>	<u>Redwood City</u>	<u>San Carlos</u>	<u>San Mateo</u>	<u>West Bay</u>	<u>Unincorporated County</u>	<u>Member Agency Total</u>
Gross Revenue Billed	\$ 3,188,740	6,558,771	10,690,190	4,594,914	5,778,606	3,151,168	10,321,736	2,695,770	18,466,567	8,228,769	21,929,464	1,504,471	3,199,374	100,308,540
Less:														
Pass-Through Costs	1,270,963	3,006,707	4,904,632	2,273,475	1,866,311	1,021,325	4,460,191	917,445	7,691,062	2,841,181	8,427,327	471,104	939,541	40,091,264
Unscheduled and Intermittent Services	<u>32,077</u>	<u>68,608</u>	<u>102,721</u>	<u>49,392</u>	<u>22,262</u>	<u>13,388</u>	<u>134,731</u>	<u>35,560</u>	<u>141,917</u>	<u>98,767</u>	<u>355,012</u>	<u>16,972</u>	<u>19,146</u>	<u>1,090,553</u>
Net Revenue Billed	1,885,700	3,483,456	5,682,837	2,272,047	3,890,033	2,116,455	5,726,814	1,742,765	10,633,588	5,288,821	13,147,125	1,016,395	2,240,687	59,126,723
Approved Contractor's Compensation	1,461,074	3,620,978	5,729,318	2,410,949	3,466,353	1,967,587	5,838,582	1,770,658	10,561,173	5,090,254	12,662,789	996,526	2,147,262	57,723,503
2013 (Surplus)/Shortfall	136,721	883,732	(41,259)	(134,974)	333,499	(356,908)	150,422	(17,634)	(144,629)	91,362	433,685	(14,775)	(117,433)	1,201,809
Interest on 2013 (Surplus)/Shortfall	8,716	56,338	—	—	—	—	9,589	—	—	5,824	—	(942)	—	79,525
Total Due Recology San Mateo County for Rate Year 2015	<u>1,606,511</u>	<u>4,561,048</u>	<u>5,688,059</u>	<u>2,275,975</u>	<u>3,799,852</u>	<u>1,610,679</u>	<u>5,998,593</u>	<u>1,753,024</u>	<u>10,416,544</u>	<u>5,187,440</u>	<u>13,096,474</u>	<u>980,809</u>	<u>2,029,829</u>	<u>59,004,837</u>
Surplus/(Shortfall) for Rate Year 2015	<u>\$ 279,189</u>	<u>(1,077,592)</u>	<u>(5,222)</u>	<u>(3,928)</u>	<u>90,181</u>	<u>505,776</u>	<u>(271,779)</u>	<u>(10,259)</u>	<u>217,044</u>	<u>101,381</u>	<u>50,651</u>	<u>35,586</u>	<u>210,858</u>	<u>121,886</u>

Note: In accordance with the Memorandum of Understanding, interest is applied to the shortfall between net revenue billed and the approved amount due Recology if rates are set below those recommended in the SBWMA report approved by the SBWMA Board. Interest is applied to 50% of the difference during the rate year in which the difference occurred (2015) because the difference occurs throughout the year and to 100% of the difference in the immediately following year (2016) because the difference exists the entire year. The interest applied to both years is the prime rate in effect when the SBWMA issued the report for that year plus one percent (1%). The prime rate for Rate Year 2015 is 3.25%.

Recology San Mateo County  
 Revenue Reconciliation  
 Rate Year 2015  
 Statement of Gross Revenue Billed

	Atherton	Belmont	Burlingame	E Palo Alto	Foster City	Hillsborough	Menlo Park	North Fair Oaks	Redwood City	San Carlos	San Mateo	West Bay	Unincorporated County	Member Agency Total	Other	Total
Revenues:																
Refuse Collection operations																
Residential	\$ 2,912,664	2,797,229	2,080,231	2,119,253	1,924,576	3,045,971	2,901,421	1,028,788	9,226,025	3,318,180	6,421,590	1,161,299	2,440,794	41,378,021	—	41,378,021
Commercial & Multi-Family Dwelling	276,001	3,476,849	6,552,072	2,179,691	3,191,135	105,197	7,174,209	1,666,982	8,144,600	4,336,763	14,256,756	329,093	758,580	52,447,928	—	52,447,928
Debris Box		218,997	1,883,047	295,832	662,895		246,106		1,095,942	577,444	1,251,026			6,231,289	—	6,231,289
Hauling revenue adjustments	(452,523)	(237,288)	27,593	37,924	(464,942)	(857,235)	55,170	26,012	(116,524)	(8,867)	(530,106)	1,501	(89,190)	(2,608,475)	—	(2,608,475)
Other	75	—	169	138	—	—	—	—	—	158	92	—	—	632	779,422	780,054
Total operating revenues	\$ 2,736,217	6,255,787	10,543,112	4,632,838	5,313,664	2,293,933	10,376,906	2,721,782	18,350,043	8,223,678	21,399,358	1,491,893	3,110,184	97,449,395	779,422	98,228,817

**RECONCILIATIONS:**

2015 revenue adjustment	(1) \$ 362,047		(21,081)	(20,411)	89,173	531,797	(282,572)	(19,247)	204,708	92,756	15,804	42,793	190,307	1,186,074	—	1,186,074
2014 (incentives)/disincentives	(444)	(1,909)	(6,337)	(3,134)	(3,022)	(496)	(4,148)	(1,520)	(10,129)	(3,485)	(11,429)	(428)	(822)	(47,303)	—	(47,303)
2014 Surplus Adjustments	(49,480)		(23,249)						18,387			(207,486)		(261,828)	—	(261,828)
2013 (surplus)/shortfall	136,721	883,732	(41,259)	(134,974)	333,499	(356,908)	150,422	(17,634)	(144,629)	91,362	433,685	(14,775)	(117,433)	1,201,809	—	1,201,809
Interest on 2013 (surplus)/shortfall	8,716	56,338	—	—	—	—	9,589	—	—	5,824	—	(942)	—	79,525	—	79,525
	457,560	938,161	(91,926)	(158,519)	419,650	174,393	(126,709)	(38,401)	68,337	186,457	438,060	(180,838)	72,052	2,158,277	—	2,158,277
Rate Stabilization account		65,696	174,671									14,079		254,446	—	254,446
Adjustment to booked 2013 (surplus)/shortfall (timing difference)	(5,037)	(700,873)	64,333	120,595	45,292	682,842	71,539	12,389	48,187	(177,590)	92,046	179,337	17,138	450,198	—	450,198
Adjustment to booked San Carlos Compactor billing										(3,776)				(3,776)	—	(3,776)
SBWMA Reimbursement of Repairs														—	(96,991)	(96,991)
SBR Fuel Revenue														—	(677,863)	(677,863)
Total Billings	\$ 3,188,740	6,558,771	10,690,190	4,594,914	5,778,606	3,151,168	10,321,736	2,695,770	18,466,567	8,228,769	21,929,464	1,504,471	3,199,374	100,308,540	4,568	100,313,108

(1) Revenue is recognized on an accrual basis when services are performed. This amount represents the difference between amounts billed and the contractual targeted compensation for services provided.

Recology San Mateo County  
 Revenue Reconciliation  
 Rate Year 2015  
 Statement of Pass-Through Costs

	Atherton	Belmont	Burlingame	E Palo Alto	Foster City	Hillsborough	Menlo Park	North Fair Oaks	Redwood City	San Carlos	San Mateo	West Bay	Unincorporated County	Member Agency Total	Other	Total
<b>Disposal Fees:</b>																
<b>Residential</b>																
MSW	\$ 157,198	306,775	344,632	631,237	295,314	212,261	406,504	260,343	933,344	399,489	1,168,276	103,726	247,117	5,466,216	—	5,466,216
Organics	674,770	358,695	443,582	333,093	234,011	394,291	707,295	182,803	1,093,908	531,991	1,204,566	218,193	365,176	6,742,374	—	6,742,374
<b>Commercial</b>																
MSW	33,892	179,171	682,105	127,960	201,150	13,288	791,467	177,219	1,307,533	501,600	1,170,301	35,065	75,914	5,296,665	27,093	5,323,758
Organics	36,363	57,270	205,450	35,776	179,829	19,172	377,689	46,252	331,866	105,504	285,089	12,233	26,368	1,718,861	—	1,718,861
<b>Multi-Family Dwelling</b>																
MSW		188,326	265,565	231,492	286,568		204,740	91,395	654,587	142,653	980,321	2,529	39,277	3,087,453	—	3,087,453
Organics		6,630	5,447	7,145	3,478		11,210	399	9,911	11,209	29,289	165	354	85,237	—	85,237
<b>Debris Box</b>																
MSW	409	44,429	728,519	83,690	102,978		46,789		364,251	79,306	388,514			1,838,885	—	1,838,885
Organics				9,951	53,269		24,017		59,549		229			147,015	—	147,015
<b>City Facilities</b>																
MSW	8,751	19,082	156,810	20,644	36,263	53,052	100,156	16,043	201,410	68,637	185,548	1,574		867,970	—	867,970
Organics	25,506	11,852	107,302	11,469	7,389	26,133	82,741	374	84,213	16,560	40,982	952	6,154	421,627	—	421,627
<b>City Self Hauled</b>																
MSW		128,152			46,780				1,705	29,821	14,156			220,614	—	220,614
Organics		11,331			6,716				13,637	453	—			32,137	—	32,137
<b>Total Disposal</b>	<b>\$ 936,889</b>	<b>1,311,713</b>	<b>2,939,412</b>	<b>1,492,457</b>	<b>1,453,745</b>	<b>718,197</b>	<b>2,752,608</b>	<b>774,828</b>	<b>5,055,914</b>	<b>1,887,223</b>	<b>5,467,271</b>	<b>374,437</b>	<b>760,360</b>	<b>25,925,054</b>	<b>27,093</b>	<b>25,952,147</b>
<b>Franchise and Other Fees</b>																
Franchise Fees	\$ 285,474	581,041	698,684	348,482	268,358	283,004	603,489	127,677	2,402,736	728,502	758,858	70,396	151,245	7,307,946	—	7,307,946
Allied Balancing Account														—	—	—
Street Sweeping Fee	24,000	394,174	234,960	232,536	94,000					89,900	320,000			1,389,570	—	1,389,570
Management Fee							300,000							300,000	—	300,000
AB939 Fee	14,000	229,935							74,096		903,000			1,221,031	—	1,221,031
Administration Fee			174,671						46,310					220,981	—	220,981
Landfill Closure Fee			436,678				749,158				978,198			2,164,034	—	2,164,034
HHW Fee	10,600	62,822	55,356		50,208	20,124	54,936	14,940	112,006	55,056		12,192	27,936	476,176	—	476,176
Rate Stabilization Fee														—	—	—
Collection Vehicle Fee		164,239												164,239	—	164,239
Litter Control Fee		131,391		200,000										331,391	—	331,391
NDPES Litter Impact Fee		65,696												65,696	—	65,696
Steam Cleaning Fee			75,000											85,000	—	85,000
Resource Conservation Fee														—	—	—
City Manager Fee			115,200											147,500	—	147,500
Asst City Manager Fee										32,300				38,200	—	38,200
Franchise and Other Fees	\$ 334,074	1,629,298	1,790,549	781,018	412,566	303,128	1,707,583	142,617	2,635,148	953,958	2,960,056	82,588	179,181	13,911,764	—	13,911,764
<b>RECONCILIATIONS:</b>																
Rate Stabilization Fee		65,696	174,671									14,079		254,446	—	254,446
Total Franchise and Other Fees	334,074	1,694,994	1,965,220	781,018	412,566	303,128	1,707,583	142,617	2,635,148	953,958	2,960,056	96,667	179,181	14,166,210	—	14,166,210
<b>Total Pass-Through Costs</b>	<b>\$ 1,270,963</b>	<b>3,006,707</b>	<b>4,904,632</b>	<b>2,273,475</b>	<b>1,866,311</b>	<b>1,021,325</b>	<b>4,460,191</b>	<b>917,445</b>	<b>7,691,062</b>	<b>2,841,181</b>	<b>8,427,327</b>	<b>471,104</b>	<b>939,541</b>	<b>40,091,264</b>	<b>27,093</b>	<b>40,118,357</b>

Recology San Mateo County  
 Revenue Reconciliation  
 Rate Year 2015  
 Statement of Revenue Billed  
 for Unscheduled and  
 Intermittent Services

	<u>Atherton</u>	<u>Belmont</u>	<u>Burlingame</u>	<u>E Palo Alto</u>	<u>Foster City</u>	<u>Hillsborough</u>	<u>Menlo Park</u>	<u>North Fair Oaks</u>	<u>Redwood City</u>	<u>San Carlos</u>	<u>San Mateo</u>	<u>West Bay</u>	<u>Unincorporated County</u>	<u>Total</u>
Revenue Billed														
Attachment Q revenues	\$ 62,506	95,744	125,411	49,483	22,262	48,231	154,635	36,184	141,917	112,112	377,400	21,504	23,037	1,270,426
Less:														
Back yard collection fees	<u>27,377</u>	<u>3,030</u>	<u>5,692</u>	<u>—</u>	<u>—</u>	<u>33,581</u>	<u>—</u>	<u>624</u>	<u>—</u>	<u>3,468</u>	<u>8,188</u>	<u>4,532</u>	<u>3,891</u>	<u>90,383</u>
Total Unscheduled Services	<u>35,129</u>	<u>92,714</u>	<u>119,719</u>	<u>49,483</u>	<u>22,262</u>	<u>14,650</u>	<u>154,635</u>	<u>35,560</u>	<u>141,917</u>	<u>108,644</u>	<u>369,212</u>	<u>16,972</u>	<u>19,146</u>	<u>1,180,043</u>
Less Included Agency Fees	3,052	24,106	16,998	91	—	1,262	19,904	—	—	9,877	14,200	—	—	89,490
Unscheduled Services less Agency Fees	\$ <u>32,077</u>	<u>68,608</u>	<u>102,721</u>	<u>49,392</u>	<u>22,262</u>	<u>13,388</u>	<u>134,731</u>	<u>35,560</u>	<u>141,917</u>	<u>98,767</u>	<u>355,012</u>	<u>16,972</u>	<u>19,146</u>	<u>1,090,553</u>

Note: Member Agencies keep the first 20% of backyard collection fees because the cost to service 20% of the customers is included in Contractor's Compensation.  
 The backyard collection fees are within the 20% threshold and therefore are reduced from the total of Unscheduled Services revenue.



Exhibit A

**MEMORANDUM OF UNDERSTANDING**

This is a Memorandum of Understanding by and between Recology San Mateo County (Recology) and the South Bayside Waste Management Authority, a California JPA (SBWMA).

A. Recology is the Franchisee for each of the twelve (12) JPA Member Agencies of the SBWMA for the collection of solid waste and recyclables pursuant to Franchise Agreements (the Franchise Agreements) entered into with each respective Member Agency.

B. Article 11 of the Franchise Agreements all provide that the SBWMA shall annually review the Recology Application for an Adjustment to Contractor's Compensation and provide a report to the SBWMA Board of Directors for consideration of a binding vote to approve the recommended Recology compensation for the subsequent rate year.

C. Article 11 of the Franchise Agreements also provides for an Annual Revenue Reconciliation that reconciles the amount owed to Recology compared to the amount retained by Recology for the prior year which generates a surplus or shortfall by agency. It also calculates interest owed to Recology for a shortfall.

D. In 2012 and 2013, the SBWMA Board approved Recology compensation for rate years 2013 and 2014, respectively, that included a reconciliation of:

1. Any surplus paid to Recology and any shortfall owed to Recology by a Member Agency for 2011 and 2012 were included in setting Recology's total compensation for 2013 and 2014, respectively.

2. Recology submitted to the SBWMA an interest calculation for both years which was charged to Member Agencies on any shortfall and credited interest to Member Agencies on any surplus. The SBWMA reports to the Board included this interest charge or credit by Member Agency in both years.

E. Recology and the SBWMA Board have reviewed their prior understanding regarding the payment of interest and reviewed the language and intent of the Franchise Agreements. Commencing with

the Recology Application, due in June 2014, for an Adjustment to Contractor's Compensation for 2015, they desire to clarify the process to calculate interest and conform to the intent of the Agreements as follows:

1. Any Member Agency that has generated a surplus balance with Recology for 2013 can receive a refund from Recology provided it requests the refund in writing on or before July 31, 2014, provided the surplus balance was generated due to the Member Agency setting rates higher than those recommended by the SBWMA. If it does not request a refund by July 31, 2014, any such surplus will be accounted for in the Recology Application for an Adjustment in Contactor's Compensation for 2015 and applied to the rate setting recommended for 2015.

2. Any Member Agency that generated a shortfall balance with Recology for 2013 will have the shortfall accounted for in the 2013 Revenue Reconciliation and recommended 2015 rates. However, if the shortfall was the result of the Member Agency setting rates lower in 2013 than had been recommended in the SBWMA Report approved by the SBWMA Board, it shall be charged the prevailing interest rate (prime plus 1%) on the shortfall balance delineated in the 2013 Revenue Reconciliation.

3. No interest will be credited to a Member Agency on any surplus balance for 2013 and in all future years. Member Agencies may request by July 31 of each year and Recology will comply with the request for a refund in a reasonable time frame. Any surplus not requested to be refunded will be credited in the next Revenue Reconciliation and applied to the next Recology Application for an Adjustment to Contractor's Compensation.

4. Recology shall not receive any interest on shortfalls in 2014 and in future years unless the Member Agency adjusts its rates below the rate adjustment recommended in the SBWMA Report and approved by the SBWMA Board.

**SBWMA**

**RECOLOGY**

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Kevin McCarthy  
Executive Director

Date

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Mario Puccinelli  
General Manager

Date



## STAFF REPORT

**To:** SBWMA Board Members  
**From:** Farouk Fakira, Finance Manager  
**Date:** July 28, 2016 Board of Directors Meeting  
**Subject:** Staff Update on 2017 Contractor Compensation Adjustment Applications

### Recommendation

This staff report is for discussion purposes only and no formal action is requested of the Board of Directors.

### Summary

This staff report provides an update on the SBWMA's review of the annual compensation adjustment applications submitted by Recology San Mateo County (Recology) and by South Bay Recycling (SBR). The SBWMA has conducted a preliminary review of the compensation application and, while there will be small change to the compensation as a result of corrections to the applications, the compensation amount estimated by Recology and SBR in their applications is not expected to change substantially.

### Analysis

#### *Recology's 2017 Compensation Application*

As prescribed in the Franchise Agreements, Recology submitted its Application for Compensation Adjustment for calendar year 2017 on June 15<sup>th</sup>; comments and questions on the application were submitted to Recology on June 29<sup>th</sup> by the SBWMA; and a revised application is to be issued by Recology on July 22<sup>nd</sup>, 2016. There were only minor changes recommended by the SBWMA (with input from the Member Agencies) to the Recology Application for Compensation Adjustment report.

The Recology 2017 compensation application indicates that the company's Total Compensation will decrease by - \$1,114,090 (-1.9% over prior year) due primarily to the below reasons (**Table 1** provides a summary of the dollar amounts of the major elements impacting the reduction in Recology's compensation adjustment for 2017).

- Lower fuel cost in 2017 due to -38.3% reduction in the Fuel Index compared to prior year.
- A scheduled reduction in Interest Expense that is -24.7% lower than prior year.
- Reduced payment to Recology of diversion based Incentive/Disincentive.

**Table 1. Summary of Recology Compensation Adjustments**

	2016	2017		
	Compensation	Compensation	Y-Y Change	% Change
Total Annual Cost of Operations	\$ 50,681,506	\$ 49,987,543	\$ (693,963)	-1.4%
Recology Profit	5,320,158	5,247,311	(72,847)	-1.4%
<i>Operating Ratio</i>	<i>90.5%</i>	<i>90.5%</i>		
Total Operating Costs	56,001,664	55,234,855	(766,810)	-1.4%
Total Contractor Pass-Through Costs	1,261,152	952,180	(308,971)	-24.5%
<b>Base Recology Compensation</b>	<b>57,262,816</b>	<b>56,187,035</b>	<b>(1,075,781)</b>	<b>-1.9%</b>
Incentive/Disincentive Payments	26,604	(11,706)	(38,309)	
<b>Total Recology Compensation</b>	<b>\$ 57,289,420</b>	<b>\$ 56,175,329</b>	<b>\$ (1,114,090)</b>	<b>-1.9%</b>

(Note: on July 8<sup>th</sup>, 2015, the Board and TAC Members were sent a revision to the Memorandum of Understanding (MOU) with Recology establishing guidelines regarding future interest calculations on surplus revenue which was previously approved by the Board at the March 17, 2014 Board meeting. This revision clarifies that interest will not be charged to a Member Agency that pays Recology by September 30 the amount of any shortfall for the previous year as determined by the Board approved Revenue Reconciliation Report).

**SBR 2017 Compensation Application**

As prescribed in the Facility Operations Agreement, SBR submitted its Application for Compensation Adjustment for calendar year 2017 on June 30<sup>th</sup>; comments and questions on the application were submitted to SBR on June 29<sup>th</sup> by the SBWMA; and a revised application is to be issued by SBR on July 22<sup>nd</sup>, 2016. There were only minor changes recommended by the SBWMA to the SBR Application for Compensation Adjustment report (no input was received from the Member Agencies).

The SBR 2017 Compensation Application indicates that the company's Total Compensation will decrease by - \$327,948 (-1.8% over prior year) due primarily to the below reasons (Table 2 provides a summary of the specific dollar amounts of the major elements impacting the reduction in SBR Compensation adjustment for 2017).

- Lower fuel cost in 2017 due to -38.3% reduction in the Fuel Index compared to prior year causing a net decrease of -6.0% in transportation cost net of labor.
- A scheduled reduction in Interest Expense that is -20.1% lower than prior year.

**Table 2. SBR 2017 Compensation Adjustment Summary**

	2016 Compensation	2017 Compensation	Y-Y Change	% Change
<b>Cost per Ton Fees</b>				
Transfer Station	\$ 12.84	\$ 12.92	\$ 0.09	0.7%
MRF (net residue)	\$ 79.76	\$ 80.67	\$ 0.91	1.1%
Transportation (cost / ton-mile)	\$ 1.08	\$ 1.02	\$ (0.06)	-6.0%
Transportation (cost / ton)	\$ 18.31	\$ 17.21	\$ (1.10)	-6.0%
<b>Total Cost Estimate by LOB</b>				
Transfer Station	\$ 4,591,441	\$ 4,621,962	\$ 30,521	0.7%
MRF (net residue)	5,903,812	5,971,246	67,433.64	1.1%
Transportation	6,548,766	6,156,049	(392,717.05)	-6.0%
Total Operating Cost	\$ 17,044,019	\$ 16,749,257	\$ (294,762)	-1.7%
<b>Pass-Through Costs</b>				
Total Interest	\$ 164,898	\$ 131,712	\$ (33,186)	-20.1%
Buyback Payment (estimate)	800,000	800,000	-	0.0%
Total Pass-Through Cost	\$ 964,898	\$ 931,712	\$ (33,186)	-3.4%
<b>Total Estimated Compensation</b>	\$ 18,008,917	\$ 17,680,969	\$ (327,948)	-1.8%

***Recology and SBR 2017 Compensation Adjustment Application Review Schedule***

Table 3 provides the complete schedule to review Recology's and SBR's compensation applications and approve the recommended rate adjustments for calendar year 2017.

<b>Due Date</b>	<b>Contractor Compensation Adjustment Process and Milestone</b>
June 15, 2016	Recology 2017 Compensation Adjustment Application submitted to MAs & SBWMA
June 29, 2016	MAs & SBWMA comments due to Recology
July 1, 2016	SBR 2017 Compensation Adjustment Application submitted to SBWMA
July 22, 2016	Revised Recology 2017 Compensation Adjustment Application submitted to MAs & SBWMA
August 12, 2016	SBWMA issues to MAs Draft Review of 2017 Recology Compensation Adjustment Application
August 15, 2016	SBWMA Issues to MAs Draft Review of 2017 SBR Compensation Adjustment Application
August 26, 2016	MAs written comments on SBWMA Draft Reports (Recology and SBR) due to SBWMA
September 8, 2016	TAC Meeting: Staff Update and discussion
September 15, 2016	SBWMA Final Reports (Recology and SBR) Issued to MAs and Board of Directors
September 22, 2016	SBWMA Board Meeting: Consideration of Final Reports

**Background**

The Franchise Agreements between the Member Agencies and Recology and the Shoreway Operations Agreement between SBR and SBWMA both prescribe the process for submittal and review of the company's applications for an annual adjustment to their compensation. The JPA is charged with performing a detailed review of the applications and providing a recommendation on the adjustment to compensation for the subsequent year for the Board's consideration at the Board meeting in September each year. In addition to the SBWMA reports providing a review of the respective contractor's compensation applications, the SBWMA also provides a report providing a projection of the base collection rate percentage adjustment needed to collect the revenues required for the next year to cover all collection costs including Recology services, disposal and processing expense at Shoreway, and agency fees paid to each Member Agency.

**Fiscal Impact**

There is an information item only and no fiscal impact is associated with this staff report.