

June 25, 2024

Mr. Eric Vail
City Attorney – City of Cathedral City
Burke, Williams, & Sorenson, LLP
submitted via email: evail@bwslaw.com

SUBJECT: Solid Waste Franchise Fee Study – R3 Report

Dear Mr. Vail,

R3 Consulting Group, Inc. (R3) is pleased to submit the attached Report of Solid Waste Franchise Fee Study (Study) to the City of Cathedral City (City). This Report presents our analytical methodology, results and findings, and recommendations regarding the solid waste Franchise Fee paid by the City's contracted solid waste collection service provider, Burrtec Waste and Recycling Services, LLC (Contractor), per the Amended and Restated Franchise Agreement for Integrated Solid Waste Management Services (Agreement) between the City and the Contractor.

The purpose of this Study was to comprehensively analyze and calculate the following:

- » **City's Costs:** The annual costs to the City for performing its management, administration, regulatory compliance and enforcement, solid waste collection and clean-up, and other obligations associated with the Contractor's Agreement and the sanitation system.
- » **Property Use Charges:** The annual use charge to the Contractor for its special and lasting access to use government property in the public right-of-way for placement of solid waste containers and collection of the solid waste contents.

We then compared the calculated values for each component to the annual Franchise Fee paid by the Contractor to the City per the Agreement. We found that the City's current and projected Franchise Fee revenues are less than the sum of the City's Costs and government Property Use Charges calculated in this Study. Based on these results, we conclude that the City's fee amount is not more than necessary to cover the City's costs in managing and administering the Agreement and the sanitation system plus the value of the Contractor's use of the public right-of-way. In a few instances where we did not receive certain variables, we estimated based on our experience elsewhere. Should you have better information, we will adjust the figures accordingly, but none are anticipated to change our main findings.

We appreciate the opportunity to be of service to the City. If you have any questions regarding this Report or need additional information, please contact me.

Sincerely,



Garth Schultz | *Principal*
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1. EXECUTIVE SUMMARY

Background

The City's Agreement with the Contractor is for the collection, processing, and disposal of solid waste from Contractor's solid waste service subscribers in the City. The Agreement provides the Contractor with the exclusive right to provide critical aspects of the City's sanitation system, including solid waste collection and the other services and programs included in the Agreement. The Agreement specifies that the Contractor will charge solid waste service subscribers, with the Contractor billing and collecting revenues from subscribers and the City authorizing the maximum rates that the Contractor may charge pursuant to the rate adjustment methodology included in the Agreement.

Per the Agreement, the Contractor pays the City a Franchise Fee to cover the costs incurred by the City in managing, administering, enforcing, and supplementing the services provided in the Agreement, as well as the charge for the use of the public right-of-way for the special and lasting access to use it for set-out and collection of solid waste containers.

Purpose

The purpose of this Study is to identify the amounts that may be reasonably recovered through the Franchise Fee paid by the Contractor to the City that are exempt from consideration as a tax. In terms of the applicable legal framework, this analysis seeks to quantify whether amounts that may be reasonably recovered through the Franchise Fees paid by the Contractors to the City fall within an exemption to the definition of a tax per Article XIII C, Section 1(e) of the California Constitution ("Proposition 26").

There are four primary exceptions to the Proposition 26 definition of tax that are relevant:

- » **Exception 1:** "A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege."
- » **Exception 2:** "A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product."
- » **Exception 3:** "A charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof."
- » **Exception 4:** "A charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property."

The Franchise Fee is a fee with two components. The first component includes the City's proportionate costs (**City's Costs**) and is a legal fee per Exceptions 1, 2 and 3. The second component includes the proportionate charges for the Contractor's use of the public right-of-way (**Property Use Charges**) and is a legal fee per Exception 4.

Methodology and Findings

To complete this Study, R3 reviewed and analyzed information provided by the City and the Contractor pertaining to the City's Costs and Property Use Charges. Using that information, we then calculated the proportionate amounts necessary to cover the City's costs, including staffing and other costs and use of government property in the public right-of-way. All calculated amounts in this Study are in current Fiscal Year (FY) 2023-24 dollars.

City's Costs

The annual costs for management, administration, regulatory compliance and enforcement, solid waste collection and clean-up, and other obligations associated with the Contractor's Agreement and the sanitation system includes: staffing salary and benefits, contracted services, capital and equipment

depreciation, operations and maintenance, supplies, and overhead for distributed costs including but not limited to property, utilities, insurance, human resources, payroll administration, accounts payable and receivable, and other finance functions.

Staffing costs are calculated based on estimated time allocations (based on historical experience and the assessment of current City employees) and other costs are calculated based on estimated share allocations associated with the sanitation system, with distributed overhead applied to both.

» The calculation results are \$386,963 in staffing costs and \$373,492 in other costs, for annual proportionate City's Costs totaling **\$760,455**.

Property Use Charges

The annual charge to the Contractor for use of government property in the public right-of-way is calculated as a function of estimates for the number of solid waste accounts setting out solid waste collection containers in the right-of-way, the set-out area used, the amount of time it is used, and the market value for the per square foot use of the public right-of-way.

» The calculation result for the use of the public right-of-way is a proportionate annual total Property Use Charge of **\$723,025**.

Conclusions

Franchise Fee

The FY 2022-23 Franchise Fee paid by the Contractor to the City was \$1,303,075 and the projection for FY 2023-24 is \$1,420,352. The sum of FY 2023-24 annual City's Costs and amounts for Property Use Charges calculated in this Study is **\$1,483,480**, which is \$63,128 (4.44%) higher than the projected FY 2023-24 Franchise Fee payments.

» The amount of the Franchise Fee is therefore not more than necessary to cover the City's costs incurred in managing and administering the Agreement and the sanitation system plus the value of the Contractor's use of the public right-of-way.

Reasonableness of Estimates and Assumptions

In performing calculations, it was necessary to estimate certain values for which reasonable ranges exist. Where assumptions were necessary for completing calculations, our objective was to apply assumptions on the lower end of the reasonable range.

Had we used other higher assumptions, the results of this Study would have been a higher calculated Franchise Fee amount. Therefore, we conclude that the calculated fee amounts are not higher than necessary to cover the City's reasonable costs plus the reasonable value of the Contractor's use of the public right-of-way.

Limitations

This Study relies on information provided by the City and the Contractor, which we have reviewed and analyzed for reasonableness and accuracy but did not independently audit or verify. As stated above, it was necessary to estimate certain values for which reasonable ranges are known to exist. Though changes to estimates and other underlying assumptions may materially change the calculations, we have elected to apply estimates on the low end of reasonable ranges, thus minimizing the potential that changes in calculations would result in different ultimate findings. We have reviewed estimates and assumptions with City staff and legal counsel and have mutual concurrence on applicability and reasonableness of all such values in this Study. Finally, the methodology employed by this Study calculates the reasonable values for the Franchise Fee within the context of current laws, regulations, and court rulings. Changes in the legal framework may require revisions to the methodology and findings contained in this Study.

2. METHODOLOGY & CALCULATIONS

City's Costs

Methodology

R3 reviewed and analyzed information provided by the City pertaining to the General Fund costs incurred for management, administration, regulatory compliance and enforcement, solid waste collection and clean-up, and other obligations associated with the Contractor's Agreement and the sanitation system.

These costs include and may not be limited to:

- » Staffing costs, including salaries and benefits.
- » Contracted services.
- » Capital and equipment depreciation.
- » Capital and equipment operations and maintenance.
- » Supplies and materials.
- » Overhead for distributed costs such as property, utilities, insurance, human resources, payroll administration, accounts payable and receivable, and other finance functions.

Using the total annual salary, benefits, and other cost information provided by the City, we estimated the proportion of costs associated with management and administration of the agreement and the sanitation system. We then calculated the proportionate totals and categorized them by the functions listed in the sections below.

Variables, Estimates and Assumptions

Staffing Costs

Variables associated with salaries and benefits include the allocation of time that positions are dedicated to management and administration of the Agreement and the sanitation system (including time supervising others with primary responsibility for these duties), the amount by which funding of salaries and benefits is paid by the General Fund, and the applicable amount of General Fund overhead.

The estimated time allocation by position category used in this Study (and based on historical experience) is shown in **Table 1**, below and on the following page, along with the explanation for the allocation values.

Table 1: Allocations of Staffing Time by Position

Positions	Time Allocation	Explanation
City Manager, Assistant City Manager, Admin Assistant, City Clerk, Admin Assistant I, Analyst I, Councilmembers.	6%	Estimated allocation for code enforcement obligations related to solid waste and sanitation services.
All Code Enforcement Positions, Assistant Facilities Maintenance Supervisor, Building Maintenance Worker II, Facilities Manager, Facilities and Field Superintendent, City Engineer, Street Maintenance Worker.	10%	Estimated allocation for code enforcement obligations related to solid waste and sanitation services.
Director of Engineering and Public Works.	20%	Estimated allocation for job obligations related to solid waste and sanitation services.

Positions	Time Allocation	Explanation
Maintenance Workers (Time on Catch Basin Waste Removal Only).	100%	Estimated allocation for portion of time spent on Catch Basin Waste Removal only.

R3 verified with City staff that the salaries and benefits included in this Study are paid by the General Fund – any non-General Fund portions of positions included in Table 1 have been excluded from the calculations. A General Fund overhead rate of 10% (to account for the for distributed costs such as property, utilities, insurance, human resources, payroll administration, accounts payable and receivable, and other finance functions) is also applied to the total allocated costs.

Other Costs

Variables associated with the City's other (i.e., non-salary and benefit) costs include the proportionate allocation of those costs that are for management and administration of the Agreement and the sanitation system, the amount by which these costs are paid by the General Fund, and the applicable amount of General Fund overhead.

The estimated time allocation by cost category used in this Study is shown in **Table 2**, below, along with the explanation for the allocation values.

Table 2: Allocations of Other Costs by Category

Cost Category	Cost Allocation	Explanation
Public Works Maintenance Crews responsible for Street Sweeping, Catch Basin Waste Removal, and Illegal Dumping Clean-up.	80%	Estimated allocation based on proportion of waste generation in City.
Tree Trimming for Large Vehicle Curbside Access in the Public Right of Way.	20%	Estimated allocation based on assumption that only 20% of tree trimming costs are related to this activity.
CalRecycle SB 1383 Compliance.	100%	All these costs are directly associated with management and administration of the Agreement and the sanitation system.

R3 verified with City staff that the other costs included in this Study are paid by the General Fund – any non-General Fund portions of these costs as included in Table 2 have been excluded from the calculations. A General Fund overhead rate of 10% (to account for the for distributed costs such as property, utilities, insurance, human resources, payroll administration, accounts payable and receivable, and other finance functions) is also applied to the total allocated costs.

Analysis

Direct Management and Administration

This category includes City staffing and consulting costs for direct management and administration of the Agreement and the sanitation system. The calculation yields \$56,031 in annual staffing costs, for total costs in this category of **\$56,031**.

Indirect Management and Administration

This category includes City staffing costs for indirect management and administration, including supervision of those responsible for direct management and administration of the Agreement and the sanitation system and associated responsibilities. The calculation yields \$72,260 in annual staffing costs, for total costs in this category of **\$72,260**.

CalRecycle and SB 1383 Compliance

This category could include City staff costs and other costs for various activities associated with the City's need to implement Senate Bill 1383 (Short-Lived Climate Pollutants Act) as well as annual reporting to the State agency CalRecycle. For the purposes of this Study, 10% of a Code Enforcement Officer I are estimated as being necessary for enforcement of the SB 1383 requirements included in the City's municipal code. The calculation yields \$11,340 in annual costs, for total costs in this category of **\$11,340**.

Code Enforcement

This category includes City staffing costs for enforcing the solid waste provisions of the City's Municipal Code, which includes illegal solid waste accumulations, illegal dumping, littering, improper waste collection setouts, nuisances, and the associated investigations, warnings, notices of violation, and administration of penalties. Total calculated annual costs in this category are **\$105,586**.

Street Sweeping

When the Contractor or individual waste generators do not properly manage the collection of solid waste, that mismanaged solid waste tends to end up in the public right-of-way and on streets, where it must be removed by the City. Street sweeping captures solid waste that ends up in public streets because of improper collection. Most, if not all, of the solid waste that ends up in the streets is generated by properties that receive solid waste collection services from the Contractor.

For the purposes of this Study, we do not assume that all mismanaged solid waste that ends up on the City's streets is generated by properties receiving solid waste services. Rather, because there is the possibility that some solid waste collected by street sweeping operations was originally generated by other sources, this Study estimates that only 80% of the solid waste collected by street sweepers was generated by properties receiving solid waste services. This assumption is consistent with other studies conducted by R3 (e.g., for the cities of Garden Grove and San Bruno) wherein street sweeping activities were allocated between 77.4% and 90% to the sanitation system.

This category includes City staffing, capital equipment, operations and maintenance, and contractor costs for the City's street sweeping operations. Total calculated annual costs in this category are **\$150,791**.

Catch Basin Waste Removal

As with street sweeping, solid waste that is not properly managed by waste generators or the Contractor, and not otherwise captured by street sweeping operations, accumulates in catch basins and other trash capture devices in the City's storm drain system. As with the street sweeping category, we do not assume that all mismanaged solid waste that ends up in catch basins or trash capture devices is generated by properties that receive solid waste services; the 80% estimate used for street sweeping costs is also applied here, and for the same reasons.

This category includes City staffing, capital equipment, and operations and maintenance costs for the City's catch basin waste removal operations. Allocated staffing costs for the Public Works maintenance crews are calculated to be \$86,170 annually. The allocated and annualized costs for capital equipment and operations, maintenance costs, and outside contractors are calculated to be \$21,140 annually, for a calculated total in this category of **\$107,310**.

Illegal Dumping Clean-up

The City's Public Works maintenance crews also clean up solid waste materials that are illegally dumped throughout the City. As with street sweeping and catch basin waste removal, an 80% waste generation allocation is applied. This category includes costs for outside contractors and service providers for clean-up of un-housed encampments. The allocated costs for clean-up of un-housed encampments are calculated to be \$176,000 annually, for a calculated total in this category of **\$176,000**.

Public Waste Containers

This category includes City staff costs and other costs for collection of waste deposited in public waste containers in the public right-of-way and other public locations in the City. The calculation yields \$43,726 in annual staffing costs, for total costs in this category of **\$43,726**.

Waste Collection at City Events

This category includes City staff costs and other costs for collection of waste generated and disposed of at City public events. The calculation yields \$23,189 in annual staffing costs, for total costs in this category of **\$23,189**.

Tree Trimming for Vehicle Access to Public Right-of-Way

This category includes contractor costs for trimming of the City's street trees to provide safe clearance for collection vehicles to collect solid waste from the public right-of-way. The calculation yields \$14,222 in annual costs, for total costs in this category of **\$14,222**.

Annual Total of City's Costs

Table 3, on the following page, shows the total of the City's Costs for management and administration of the Agreement and the sanitation system as calculated in this Study, by category.

Table 3: City's Annual Costs by Category and in Total

Category	Staffing Costs	Other Costs	Total
Direct Management and Administration	\$56,031	-	\$56,031
Indirect Management and Administration	\$72,260	-	\$72,260
CalRecycle SB 1383 Compliance	-	\$11,340	\$11,340
Code Enforcement	\$105,586	-	\$105,586
Street Sweeping	-	\$150,791	\$150,791
Catch Basin Waste Removal	\$86,170	\$21,140	\$107,310
Illegal Dumping Clean-up	-	\$176,000	\$176,000
Public Waste Containers	\$43,726	-	\$43,726
Waste Collection at City Events	\$23,189	-	\$23,189
Tree Trimming	-	\$14,222	\$14,222
Total Annual City's Costs	\$386,963	\$373,492	\$760,455

Property Use Charges

Methodology

R3 reviewed and analyzed information provided by the City and the Contractor pertaining to Property Use Charges for Contractor's use of the public right-of-way for collection of solid waste collection containers. They then calculated the annual Property Use Charges based on:

- » The setout area used for collection of solid waste containers (in square feet).
- » The amount of time that the area is used.
- » The market value for use of the public right-of-way (in dollars per square foot).
- » The number of solid waste subscribers setting out collection containers in the public right-of-way.

Using these values, we calculated the market value for the Contractor's use of government property in the City.

Variables, Estimates, and Assumptions

Setout Area

Standard residential solid waste collection setouts include three solid waste collection containers, usually carts with wheels and lids, with one each for garbage, recycling, and organics waste streams. The setout area needed for placement of these containers is inclusive of the width of each container (typically two feet) as well as minimum required space between the containers and other objects such as cars (minimum of one foot). The set-out area also takes up available parking space and is, thus, assumed to extend six feet out from the curb. Taken altogether, the area for residential setouts is calculated as three containers that are each two feet wide, plus one foot between each container and other objects, for a total area ten feet wide times six feet in depth. The result is 60 square feet of setout area per serviced single-family residential property.

The amount of area used for commercial setouts (in this Study, use of the term commercial also always includes multi-family) can vary widely, as there is no standard commercial subscription size profile – each commercial solid waste subscriber can select from a range of container sizes, with most of them being larger than the containers used in residential areas. Given this complexity, this Study assumes that the average commercial setout area is twice that of the residential setout area, for 120 square feet. This estimate is likely lower than the average setout area needed in commercial areas and is, therefore, conservative.

Setout Time Usage

Standard residential solid waste collection is performed once weekly. Most residential containers are set out the evening prior to collection and are removed from the public right-of-way the following afternoon. Thus, for the purposes of this Study, we assume that collection containers are in the public right-of-way for an average of 18 hours per day, one day per week, which amounts to approximately 10.71% of the time (18 hours divided by 24 per day divided by 7 days per week).

Commercial solid waste subscription setout times can vary widely – just as there is no standard commercial subscription size profile, likewise there is no standard collection frequency. Commercial solid waste subscribers can select collection frequency between once and six times per week, and with different frequencies for different waste streams. Given this complexity, this Study assumes that the average commercial collection frequently is twice weekly, for 21.42% of the time. As with the setout area, this estimate is likely lower than the average commercial collection frequency and is, therefore, conservative.

Market Value for Use of Public Right-of-Way

To establish a market value for use of the public right-of-way, R3 conducted an online survey of recent purchases of bare land in and around the City. R3 found 30 recent sales of bare land with a median sale value of \$34.89 per square foot. To that value, R3 added the per square foot replacement value of the City's street pavement, which is calculated as a function of the total replacement value of the City's streets (\$341,800,000) divided by the area of the streets in square feet (35,537,844) both of which are contained in the City's 2023 Pavement Management Program report. The resultant value of the street improvements (meaning the value of the existing pavement system, not the value of projected future capital projects and maintenance required to maintain the value of the pavement system) is \$9.62 per square foot, which, when added to the \$34.89 market value of bare land, yields \$44.51 per square foot.

This value is then divided by a rental realization rate of 7.2, which was derived based on the ratio of the \$44.51 per square foot "purchase value" compared to 29 market rates for rental of bare land for parking.

The result is multiplied by the General Fund overhead rate of 10% to account for distributed costs including but not limited to property, utilities, insurance, human resources, payroll administration, accounts payable and receivable, and other finance functions, with the resulting per square foot value of \$6.80.

This value is comparatively low given other methods that we could have used. For example, other communities have established use charges for use of the public right-of-way via “Streeter” programs or parklet rentals. To our knowledge, the minimum annual use charge per square foot in these communities is \$5.21 and the largest is \$30.00. The average annual per square foot use charge in these communities is \$15.67.

Number of Subscriptions Setting Out Containers

The City reports that there are 18,198 residential and 826 commercial solid waste service subscribers in the City. However, not all subscribers set out their containers in the public right-of-way for collection all the time.

To account for non-setouts (either because subscribers don’t have waste materials to set out or because they receive on-premises service) we assume that only 90% of residential solid waste subscribers set out containers on a regular basis, for a resulting total of 16,378 average residential setouts. It is also understood that most commercial subscribers do not set out containers in the public right-of-way, and therefore we conservatively assume that only 5% of commercial subscribers set out containers on a regular basis, for a resulting total of 41 average commercial setouts.

It should be noted that the 90% set-out estimate for residential customers may be low, and the 5% set-out rate for commercial customers is almost certainly low – were one to take field observations for these values, we believe that the actual rates of set-out would be higher than used for the purposes of this Study.

Analysis and Total Annual Property Use Charges

Calculating the total annual Property Use Charges using the variables, estimates, and assumptions from the prior section is a function of multiplication, as shown in **Table 4**, below.

Table 4: Calculation of Total Annual Property Use Charges

Variable Category	Residential	Commercial	Grand Total Annual Property Use Charge
Setout Area	60 SF	120 SF	
Setout Time Usage	10.71%	21.42%	
Annual Use Charge	\$6.80 per SF	\$6.80 per SF	
Number of Setouts	16,378	41	Grand Total Annual Property Use Charge
Total Annual Property Use Charges	\$715,857	\$7,168	

3. FINDINGS & CONCLUSIONS

Franchise Fee

- » The FY 2022-23 Franchise Fee paid to the City was \$1,303,075 and the projection for FY 2023-24 is \$1,420,352.
- » R3 calculated estimates of the City's Costs and Property Use Charges based on actual and estimated cost information provided by the City, and with conservative assumptions for estimated values.
- » The sum of FY 2023-24 annual City's Costs (\$760,455) and Property Use Charges (\$723,025) amounts calculated in this Study is \$1,483,480.
- » Where assumptions were necessary to complete the analysis in this Study, reasonable attempts were made to apply conservative assumptions given a range of possible inputs.
- » The calculated amounts bear a reasonable relationship to the Contractor's burdens on the City resulting from the management and administration of the Agreement and the sanitation system, and the reasonable value of the Contractor's use of the public right-of-way. The City's Costs have been reviewed and confirmed by City staff as being representative of the actual time and costs incurred for these activities. Amounts of Property Use Charges are proportionately allocated to the Contractor with due recognition of the realities of the Contractor's operations.
- » The amounts calculated in this Study are \$63,128 (4.44%) higher than the projected FY 2023-24 Franchise Fee payments. It is highly unlikely, given the justification provided herein, that FY 2023-24 Franchise Fee payments will exceed the amounts calculated in this Study.
- » The projected FY 2023-24 Franchise Fee is less than would be justified by the calculations in this Study.
- » The Franchise Fee therefore is not more than necessary to cover the City's costs incurred in managing and administering the Agreement and the sanitation system plus the value of the Contractor's use of the public right-of-way.

4. RECOMMENDATIONS

Annual Adjustments

All values calculated in this Study are in current FY 2023-24 dollars. Given that the City's Costs and Property Use Charges will tend to change over time in response to changing staffing, benefits, and other costs, it would be appropriate for the City to implement an annual adjustment to the Franchise Fee.

- » R3 recommends the City consider including an automatic annual adjustment that would change the fees in proportion to the percentage change in the Consumer Price Index (CPI). We recommend the CPI for All Urban Consumers (CPI-U) for the Los Angeles-Long Beach-Anaheim area (U.S. Bureau of Labor Statistics series ID: CUURS49ASA0).

Sources and Uses Accounting

Currently, the City's Costs and Property Use Charges are not tied to Franchise Fee revenues in the City's accounting system. The City could implement project code accounting and/or enterprise fund accounting for the Franchise Fee to better track source revenues and their uses. In either case, allocated and/or direct staffing and other costs could be tied to source revenues, while the Property Use Charges could be transferred out for general use.

- » R3 recommends the City consider implementing sources and uses accounting practices for Franchise Fee revenues, City's Costs, and Property Use Charges.

Periodic Recalculation

Over time, the City's Costs associated with the Agreement and the sanitation system and the value of Property Use Charges for use of the public right-of-way may change in ways that vary from the annual change in the CPI. Additionally, changes in City policies, programs, procedures, organization, geopolitical boundaries, laws, regulations, court rulings, and/or other factors may also trigger a need for recalculating fees.

- » R3 recommends the City consider updating this Study periodically (e.g., every five years) or more frequently if needed to recalculate fees in response to other factors.