

Solid Waste 2-Year Rate Proposal

Effective January 1, 2020 and January 1, 2021

1. Proposed Rate Increases:

	Salem-Marion County				Salem-Polk County			
Effective 1/1/2020	Combined	Cart	Container	Rolloff	Combined	Cart	Container	Rolloff
Year-1 Rate Increase	3.00%	4.25%	0.00%	4.19%	5.50%	5.00%	7.18%	11.50%
Target Return on Revenue 8-12%	9.9%	9.7%	10.3%	9.7%	9.3%	9.5%	8.5%	9.4%
Effective 1/1/2021	Combined	Cart	Container	Rolloff	Combined	Cart	Container	Rolloff
Year-2 Rate Increase	3.00%	4.25%	1.46%	2.31%	5.50%	5.00%	7.50%	10.00%
Target Return on Revenue 8-12%	10.8%	11.3%	10.1%	10.6%	11.5%	11.3%	12.2%	11.4%
Residential 35-Gallon Cart	Cart				Cart			
Year-1 Annual Increase	\$ 15.00				\$ 14.40			
Year-2 Annual Increase	\$ 15.60				\$ 15.00			

2. Expenditure Growth Assumptions:

	Salem-Marion County			Salem-Polk County		
	2019	2020	2021	2019	2020	2021
Personnel	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Medical Insurance	5.00%	4.30%	4.30%	5.00%	4.30%	4.30%
Fuel	-5.70%	9.40%	5.00%	-5.70%	9.40%	5.00%
Disposal	1.94%	1.00%	0.18%	8.02%	2.40%	1.54%
Garbage - Covanta rates	0.00%	0.00%	0.00%			
	\$ 87.45	\$ 87.45	\$ 87.45			
Garbage - Coffin Butte rates				4.76%	0.00%	2.74%
				\$ 33.00	\$ 33.00	\$ 33.93
Yard Debris / Kitchen Waste rates		9.21%	1.61%		9.21%	1.61%
	\$ 55.38	\$ 61.00	\$ 62.00	\$ 55.38	\$ 61.00	\$ 62.00
Commingled Recycling rates	23.12%	0.00%	0.00%	23.12%	0.00%	0.00%
	\$ 104.38	\$ 104.38	\$ 104.38	\$ 104.38	\$ 104.38	\$ 104.38
General Inflation	2.81%	2.81%	2.81%	2.81%	2.81%	2.81%
Depreciation - Vehicles	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
HB 3427 Gross Receipts Tax	\$ -	\$ 139,000	\$ 143,000	\$ -	\$ 15,130	\$ 16,000

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3. The Disposal for Carts in Marion County is 31% of Total Operating Costs, However, only 18% of Total Cost is Covanta

Marion County Disposal as a % of Total Cost

	Cart	Container	Rolloff
Garbage (Covanta)	18%	39%	60%
Yard Debris / Kitchen Waste	8%	0%	0%
Commingled Recycling	5%	3%	0%
Total Disposal	31%	41%	60%

4. Tonnage Trend (Recycling Decline):

Total Solid Waste Volume for Carts and Containers							
Year	Garbage	YoY	Commingled Recycling	YoY	Total	YoY	Recycle % of Total
2015	119,529		21,838		141,367		15.4%
2016	127,202	6%	22,549	3%	149,751	6%	15.1%
2017	131,716	4%	24,780	10%	156,496	5%	15.8%
2018	133,617	1%	19,821	-20%	153,438	-2%	12.9%

5. What if no rate increase was approved (0.00%) would the City achieve its SRC "reasonable" Return on Revenue target of 10%? No, as follows:

	Salem-Marion County				Salem-Polk County			
Effective 1/1/2020	Combined	Cart	Container	Rolloff	Combined	Cart	Container	Rolloff
Year-1 Rate Increase	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Target Return on Revenue 8-12%	7.4%	6.2%	10.3%	6.3%	4.7%	5.3%	2.5%	4.2%
Effective 1/1/2021	Combined	Cart	Container	Rolloff	Combined	Cart	Container	Rolloff
Year-2 Rate Increase	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Target Return on Revenue 8-12%	5.8%	4.3%	8.9%	5.3%	2.3%	3.0%	0.0%	1.5%

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6. How did Salem arrive at a 10% pre-tax profit margin target? How do other cities arrive at their rate structures, do they use the same 10% target?

- ORS 459.017 (b) gives local jurisdictions the primary responsibility for solid waste management.
- ORS 459A.085(3) provides legislative intent “that a city or county may displace competition with a system of regulated collection service by issuing franchises which may be exclusive if service areas are allocated.” Further
- SRC 47.099 (f) (5) notes that rates must be adjusted to yield a “**reasonable operating margin**” for the haulers. For decades Salem has targeted a pre-tax margin of 10% for Salem haulers. If the pre-tax margin is below a range of 8%-12%, rates are adjusted.

The pre-tax margin sometimes called a Return on Revenue (ROR) is calculated by subtracting Allowable Expenses from Total Revenue to determine Franchise Income. Franchise Income is then divided by Total Revenue to determine the ROR.

- $\text{Total Revenue} - \text{Allowable Expenses}^* = \text{Franchise Income}$
- $\text{Franchise Income} / \text{Total Revenue} = \text{Return on Revenue}$

**Some expenses such as donations and executive life insurance are excluded from the calculation.*

Chris Bell and Associates produced the following table in 2013 for the Oregon Refuse and Recycling Association (ORRA) outlining the top 10 populated cities in Oregon and their target operating margins. Gresham has since codified its target margin to be 10% and Beaverton’s code targets 9%. From this margin, haulers pay local, state and federal taxes (approximately 3%). Another 3% is allocated to reserves used to run the day to day activities of the business. The remaining 4% is passed back to the owners in the form of dividends and distributions, which are again taxed as income.

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Current Operating Margin for SW in Oregon's 10 Largest Cities

Rank	City	Rate Method	Target Margin	Market Type
1	Portland	Annual Review	9.50%	Residential Franchise
2	Eugene	Annual Review	11%	Open Mkt. w/ License
3	Salem	Annual Review	10%	Franchised Areas
4	Gresham	Annual Review	?	Franchised Areas
5	Hillsboro	Annual Review	8%	Franchised Areas
6	Beaverton	Annual Review	9%	Franchised Areas
7	Bend	Annual Review	10%	Franchised Area
8	Medford	CPI / Request	8 to 10%	Franchised Area
9	Springfield	Rate Request	8 to 11%	Franchised Area
10	Corvallis	Annual Review	8 to 10%	Franchised Area

ORRA Rate of Return – Rate Setting
March 7, 2013 10/9/2019

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7. What has been the Haulers' 5-year income trend? How much are they bringing in compared to the 10% targeted rate of return?

Below are two tables: the first showing the financials for the haulers as a composite in Marion County and the second for Polk County. The bottom blue row shows the actual pre-tax margin experienced by the haulers for each year. It is important to note that while rates are set to target a 10% pre-tax margin, there is no true-up for haulers if the actual margin falls below the target.

City of Salem (Marion County) Cost of Service Analysis

	2018		2017		2016		2015		2014		2013
	TOTAL	YoY	TOTAL	YoY	TOTAL	YoY	TOTAL	YoY	TOTAL	YoY	TOTAL
TOTAL REVENUE	\$ 26,987,957	4.1%	\$ 25,926,265	14.8%	\$ 22,577,818	8.8%	\$ 20,749,909	7.6%	\$ 19,290,671	1.5%	\$ 18,999,319
DIRECT COST OF OPERATIONS	\$ 22,369,776	7.3%	\$ 20,847,529	16.9%	\$ 17,829,881	9.3%	\$ 16,319,022	7.4%	\$ 15,192,127	2.4%	\$ 14,837,039
GROSS PROFIT	\$ 4,618,180	-9.1%	\$ 5,078,736	7.0%	\$ 4,747,938	7.2%	\$ 4,430,886	8.1%	\$ 4,098,544	-1.5%	\$ 4,162,280
TOTAL G&A EXPENSES	\$ 2,943,887	-2.9%	\$ 3,032,461	8.1%	\$ 2,805,596	3.7%	\$ 2,704,825	4.0%	\$ 2,601,095	10.1%	\$ 2,362,935
INCOME FROM OPERATIONS	\$ 1,674,293	-18.2%	\$ 2,046,275	5.4%	\$ 1,942,341	12.5%	\$ 1,726,062	15.3%	\$ 1,497,449	-16.8%	\$ 1,799,344
TOTAL ADJUSTMENTS	\$ (662)		\$ (455)		\$ (455)		\$ 3,638		\$ 271		\$ 156
FRANCHISE INCOME	\$ 1,673,632	-18.2%	\$ 2,045,820	5.4%	\$ 1,941,886	12.3%	\$ 1,729,700	15.5%	\$ 1,497,720	-16.8%	\$ 1,799,500
FRANCHISE MARGIN	6.2%		7.9%		8.6%		8.3%		7.8%		9.5%

Note: Years 2013 - 2017 were prepared by Dan Porth, CPA. These figures were provided by his office and have not been verified or audited in any way.

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City of Salem (Polk County) Cost of Service Analysis

	2018		2017		2016		2015		2014		2013
	TOTAL	YoY	TOTAL	YoY	TOTAL	YoY	TOTAL	YoY	TOTAL	YoY	TOTAL
TOTAL REVENUE	\$ 3,093,277	3.1%	\$ 3,001,543	5.1%	\$ 2,856,036	4.2%	\$ 2,740,796	7.9%	\$ 2,539,898	2.8%	\$ 2,470,682
DIRECT COST OF OPERATIONS	\$ 2,602,441	13.8%	\$ 2,285,943	9.8%	\$ 2,081,390	3.0%	\$ 2,020,230	1.9%	\$ 1,981,648	0.0%	\$ 1,981,997
GROSS PROFIT	\$ 490,835	-31.4%	\$ 715,600	-7.6%	\$ 774,646	7.5%	\$ 720,566	29.1%	\$ 558,251	14.2%	\$ 488,685
TOTAL G&A EXPENSES	\$ 465,551	7.0%	\$ 435,046	2.6%	\$ 424,103	5.1%	\$ 403,665	7.8%	\$ 374,331	4.4%	\$ 358,603
INCOME FROM OPERATIONS	\$ 25,284	-91.0%	\$ 280,555	-20.0%	\$ 350,543	10.6%	\$ 316,901	72.3%	\$ 183,920	41.4%	\$ 130,082
TOTAL ADJUSTMENTS	\$ -		\$ -		\$ -		\$ -		\$ (8,086)		\$ 2,219
FRANCHISE INCOME	\$ 25,284	-91.0%	\$ 280,555	-20.0%	\$ 350,543	10.6%	\$ 316,901	80.2%	\$ 175,834	32.9%	\$ 132,301
FRANCHISE MARGIN	0.8%		9.3%		12.3%		11.6%		6.9%		5.4%

Note: Years 2013 - 2017 were prepared by Dan Porth, CPA. These figures were provided by his office and have not been verified or audited in any way.

8. Is Salem's rate methodology of avoiding preferences between product lines a practice or policy? For example, can we reduce residential (cart) rates by increasing commercial (container) rates?

SRC 47.015 (b) states that part of the responsibility of solid waste management is to "prohibit rate preferences and other discriminatory practices."

Staff interprets this language to mean that through the management of solid waste, the City is not to show preferable rate adjustments whether by hauler or by line of business (e.g. residential v. commercial).

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9. What if the City were to propose a flat increase for each year by County?

Solid waste services are provided by six companies within Salem. Each of these companies services an exclusive territory within the city and therefore have varying mixes of customer bases (e.g., residential vs. commercial). In order to avoid rate preferences from one line of business to another, or from one customer type to another, Salem has a practice of targeting the 10% margin, not only by zone (Marion and Polk counties), but also by line of business (cart, container, and rolloff). This practice helps to ensure that no one hauler is given preference over another and that one group of customers isn't given preference over another. In general, artificially adjusting rates to flatten increases year-over-year should be avoided unless the pre-tax margin of 10% (or at least within the range of 8%-12%) can be maintained for each line of business.

10. Describe Salem's process for analyzing vendor financials and rate increase requests along with Salem's engagement of a professional third party to assist in these analyses.

During the rate setting process, haulers individually submit their most recently completed financials and their year-end projections for the current year to the City and/or the City's consultant. The haulers also provide important qualitative metrics like tonnage, disposal rates, fuel prices and the number/type of customer accounts which impact incomes. This information is reviewed and analyzed by staff and the consultant and then the haulers and the City meet to discuss their proforma. Using all this information, the City creates a suggested rate recommendation to the Council for approval in such a way that rates are "just, fair, reasonable and adequate" as described in SRC 47.015 (d)

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11. What have been the changes to the market recently in solid waste/recycling that have caused rate increases higher than anticipated?

Higher than anticipated rate increases in recent years are largely due to a significant downturn in the recycling commodities market, which local haulers and processors have no control over. Historically, the sale of recycled material collected by haulers in curbside carts and containers, and metals recovered from the ash at the Covanta burner helped to offset customer rates. As the value of these recycled and recovered materials dropped, the offset to customer rates disappeared.

- In 2016 staff reported that:
 - Lower demand overseas resulting in a reduction of recyclable material purchased by China significantly impacts demand and pricing in the United States. Most market forecasters predict the average value for recyclable material will be lower over the next five years as compared to the previous five years.
 - Low oil prices reduce the price of virgin plastic, which in turn, reduces the demand for recycled plastic.
 - Paper pricing had declined over the last year due to further mill closures, including the last local newspaper mill in Newberg, Oregon. China's lower demand has also caused fiber pricing to drop significantly over the last year.
 - The price for recycled steel has hit historic lows due to China's significant reduction in demand, as well as a reduction in demand domestically. There is also excess smelting capacity worldwide that is driving down aluminum and other non-ferrous metal prices. Domestic prices for recyclable metal dropped approximately 85 percent over the last two years.

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- January 2018, China's announced that as of January 1, 2018 they would no longer accept material that has more than 0.5% contaminate level. With existing technology, reducing contaminants to this level was not cost effective and remains so today. At the time, approximately half of all recycled material was sent to China.
- By the end of 2018, haulers were paying nearly \$85 per ton to dispose of commingled recycled material, when in 2017 they were being paid an average \$0.33 cents per ton.
- In 2019:
 - Comingled recycling now costs haulers over \$100 per ton and as much as \$110 in the last quarter of 2019.
 - Cardboard, which was the last recycled commodity to have value has also dropped to nearly no value. Haulers currently receive less than \$10 per ton but averaged almost \$30 per ton in 2018. Domestically, cardboard is being stockpiled as there is reduced demand.
 - Metal, which recovered some since 2016, dropped 45% year over year from an average of \$225.90 per ton in 2018 to \$125.00 per ton in 2019.

Even though the cost of processing and disposing of commingled recycling material is greater than garbage, Oregon state law requires all cities with a population of over 4,000 to offer curbside recycling.

12. What is the recent history of operational and cost for the Covanta facility?

- Marion County and Covanta extended current contract for one year to accommodate further legislative efforts to qualify Covanta as a source of sustainable energy.

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Franchise Solid Waste Rates by Jurisdiction

Residential-20 Gal

Jurisdiction	2016	2017	YoY	2018	YoY	2019*	YoY	Proposed 2020	YoY	Proposed 2021	YoY
Springfield	\$11.65	\$11.95	2.6%	\$13.31	11.4%	\$13.36	0.4%				
Eugene	\$11.80	\$11.80	0.0%	\$14.45	22.5%	\$14.45	0.0%				
Salem-Polk	\$19.95	\$20.10	0.8%	\$18.10	-10.0%	\$21.15	16.9%	\$22.20	5.0%	\$23.30	5.0%
Corvallis	\$17.84	\$18.19	2.0%	\$20.92	15.0%	\$22.00	5.2%				
Hillsboro	\$19.10	\$19.10	0.0%	\$21.80	14.1%	\$22.29	2.2%				
Kelzer	\$19.30	\$20.27	5.0%	\$20.27	0.0%	\$24.62	21.5%				
Beaverton	\$22.05	\$22.05	0.0%	\$24.70	12.0%	\$24.70	0.0%				
Salem-Marion	\$19.95	\$22.85	14.5%	\$23.55	3.1%	\$26.30	11.7%	\$27.40	4.2%	\$28.55	4.2%
Gresham	\$25.91	\$25.91	0.0%	\$28.24	9.0%	\$28.24	0.0%				
Medford	N/A	N/A	N/A	N/A	N/A	N/A	N/A				

Residential-35 Gal

Jurisdiction	2016	2017	YoY	2018	YoY	2019*	YoY	Proposed 2020	YoY	Proposed 2021	YoY
Springfield	\$16.60	\$17.00	2.4%	\$18.90	11.2%	\$19.00	0.5%				
Medford	\$17.03	\$19.08	12.0%	\$19.44	1.9%	\$20.30	4.4%				
Salem-Polk	\$20.25	\$20.40	0.7%	\$20.65	1.2%	\$23.85	15.5%	\$25.05	5.0%	\$26.30	5.0%
Corvallis	\$19.89	\$20.28	2.0%	\$23.09	13.9%	\$24.30	5.2%				
Eugene	\$21.50	\$21.50	0.0%	\$24.65	14.7%	\$24.65	0.0%				
Hillsboro	\$22.85	\$22.85	0.0%	\$25.75	12.7%	\$26.24	1.9%				
Kelzer	\$21.45	\$22.52	5.0%	\$22.52	0.0%	\$27.13	20.5%				
Beaverton	\$25.20	\$25.20	0.0%	\$27.85	10.5%	\$27.85	0.0%				
Salem-Marion	\$22.25	\$25.85	16.2%	\$26.65	3.1%	\$29.50	10.7%	\$30.75	4.2%	\$32.05	4.2%
Gresham	\$29.69	\$29.69	0.0%	\$32.36	9.0%	\$32.36	0.0%				

Commercial-2 Yard

Jurisdiction	2016	2017	YoY	2018	YoY	2019*	YoY	Proposed 2020	YoY	Proposed 2021	YoY
Salem-Polk	\$87.05	\$87.95	1.0%	\$91.20	3.7%	\$99.40	9.0%	\$106.55	7.2%	\$114.55	7.5%
Salem-Marion	\$113.25	\$126.20	11.4%	\$126.20	0.0%	\$132.90	5.3%	\$132.90	0.0%	\$134.85	1.5%
Kelzer	\$123.11	\$129.27	5.0%	\$129.27	0.0%	\$138.97	7.5%				
Gresham	\$156.02	\$156.02	0.0%	\$156.02	0.0%	\$156.02	0.0%				
Corvallis	\$139.87	\$142.57	1.9%	\$148.60	4.2%	\$156.39	5.2%				
Hillsboro	\$135.44	\$135.44	0.0%	\$157.13	16.0%	\$157.13	0.0%				
Beaverton	\$147.56	\$147.56	0.0%	\$168.81	14.4%	\$168.81	0.0%				
Eugene	\$142.45	\$142.45	0.0%	\$174.75	22.7%	\$174.75	0.0%				
Springfield	\$174.70	\$178.85	2.4%	\$198.70	11.1%	\$199.95	0.6%				
Medford	\$148.61	\$166.54	12.1%	\$169.7	1.9%	\$216.58	27.6%				

* Sorted lowest to highest on 2019 rates

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