



**CITY OF KIRKLAND**  
Department of Public Works  
123 Fifth Avenue, Kirkland, WA 98033 425.587.3800  
www.kirklandwa.gov

---

## MEMORANDUM

**To:** Kurt Triplett, City Manager

**From:** Julie Elsom, Senior Operations and Financial Analyst  
Ray Steiger, P.E., Public Works Director

**Date:** August 27, 2012

**Subject:** Proposed 2013-2014 Utility Rates

### **RECOMMENDATION:**

It is recommended that the Council review the proposed 2013-2014 utility rates and provide staff direction on final adoption of the rates at the September 18 Council meeting.

### **BACKGROUND AND DISCUSSION:**

This memorandum provides an overview of the proposed utility rates for 2013 and 2014. The utility rates which include: water, wastewater, solid waste, and surface water were last presented to the City Council finance committee on August 20, 2012, and their feedback and recommendations are incorporated herein. Based on the full Council feedback and direction, Public Works will present the final rates to the Council for their adoption at their September 18<sup>th</sup> meeting. Council action must be taken on Solid Waste rates on or before the October 16, Council meeting in order for these rates to be effective January 1, 2013.

Specific issues discussed as a part of the 2013/2014 rates include:

- The required modification in utility tax accounting discussed at the July 17, 2012 Study Session. Recommendations in the memo are based on direction given to reduce the City utility tax rate identified in the Kirkland Municipal Code to neutralize the impact of the accounting change to the customer and the General Fund. A more complete discussion of this issue by Finance Director Tracey Dunlap is included as Attachment I.
- Continued progress towards recommended funding levels that will fully account for depreciation of assets (also referred to as system reinvestment funding). The City's system replacement funding policy is based in part on the FCS Group's 2007 long-term water/wastewater rate study; the Study recommended the amount of annual rate funding necessary to fund replacement of the system over a 50-year period. Assuming a long term debt to capital ratio of 25% debt/75% cash target multipliers applied to the depreciation expense were recommended as follows: water 1.25, and wastewater 1.65. The surface water multiplier is currently being reviewed as part of the master plan update. Solid waste does not include City depreciation funding; however, a \$300,000

per year fee is included for street preservation. The surface water, water and wastewater utilities are currently funding system reinvestment at a depreciation multiplier of 1.0.

*Water*

The 2012 monthly water rate is \$36.86 for a typical single family; the utility tax rate is 13.38%.

The water utility provides for construction, replacement and rehabilitation of water distribution and storage facilities, funds the purchase of water from the Cascade Water Alliance (CWA), and provides for ongoing maintenance and operations of the water utility infrastructure. City participation in CWA allows Kirkland to have a voice and a vote over reliable and adequate drinking water supplies. Approximately 54% of the Utility's annual operating expenditures are payments to CWA for the purchase of water, and preliminary rate increases proposed by CWA for Kirkland are:

2013	2014
3.40%	7.40%

Major drivers for changes to CWA rates are:

- CWA Operating Budget *reductions*:
  - Lake Tapps operations \$852K
  - Conservation program changes \$420K
  - General operations /other \$124K
- CWA Operating Budget *additions*:
  - Wholesale water contract costs increased \$1.6 M
  - Salary & Benefits \$335K
- Other *additions*:
  - Growth projections continue downward so revenue is below projections
  - Anticipated bond issuance

Kirkland's direct costs for maintenance and operations account for the remaining 46% of the annual expenditures. Drivers of the 2013/2014 rate proposal are:

- An incremental increase of .05 for system reinvestment funding; the current level of 1.0 will be 1.05 in 2013 and 1.10 in 2014; the 1.25 target is scheduled to be met in 2017.
- Recent Federal Unregulated Contaminant Monitoring Rule (UCMR 3) has caused an increase in water maintenance needs.

As a result of these elements, the preliminary 2013-2014 water rates increase as follows:

Rate element	2013 (%)	2014 (%)
CWA	1.99	4.19
State tax on City tax	0.66	0.00
<i>Subtotal – Pass thru</i>	<i>2.65</i>	<i>4.19</i>
Phasing in System Reinvestment	0.72	0.68
<i>Cumulative Rate Increase</i>	<i>3.37</i>	<i>4.87</i>

Leading to a typical single family monthly rate:

2012	2013	2014
\$ 36.86	\$ 38.10	\$ 39.96

Resulting in a proposed single family monthly rate with utility tax included:

	2012	2013	2014
Typical Monthly Bill	\$36.86	\$38.10	\$39.96
Utility Tax impact	\$4.93	\$5.10	\$5.34
Total Bill:	\$41.79	\$43.20	\$45.30

*Finance Committee Recommendation*

Approve proposed water rates for 2013 and 2014.

*Wastewater*

The 2012 wastewater rate is \$61.48 for a typical single family; the utility tax rate is 10.50%.

The wastewater utility provides for Kirkland's share of regional wastewater collection, treatment, disposal, and bio-solids reuse program administered by King County DNR. In addition, it provides for construction, operation, and maintenance of the City's wastewater collection system. Approximately 62% of the City's total budgeted operating expenditures are payments to KCDNR. The King County Council is proposing a monthly wholesale rate increase of:

2013	2014
10.39%	0.00%

This equates to \$39.85 per month for 2013 and 2014; the 2012 rate is \$36.10 per month.

Drivers for KCDNR rate *increases* are:

- Continued borrowing to finance construction projects, and
- Growth in the region is significantly down from prior projections so revenue is down.

Kirkland's direct costs for maintenance and operations account for the remaining 38% of annual expenditures. Drivers of the 2013/2014 rate proposal are:

- An incremental increase of .10 for system reinvestment funding; the current level of 1.0 will be 1.10 in 2013 and 1.20 in 2014 at 1.20; the 1.65 target is scheduled to be met in 2019.
- An increase in communications costs of approximately \$11,000 annually for telemetry at wastewater lift stations.

As a result of these elements, the preliminary 2013-2014 waste water rates increase as follows:

Rate element	2013 (%)	2014 (%)
King County DNR	6.46	0.00
State tax on City tax	0.36	0.00
<i>Subtotal – Pass thru</i>	<i>6.82</i>	<i>0.00</i>
Phasing in System Reinvestment	0.00	0.00
<i>Cumulative Rate Increase</i>	<i>6.82</i>	<i>0.00</i>

Leading to a typical single family monthly rate:

2012	2013	2014
\$ 61.48	\$ 65.47	\$ 65.47

Resulting in a proposed single family monthly rate with utility tax included:

	2012	2013	2014
Typical Monthly Bill	\$61.48	\$65.47	\$65.47
Utility Tax impact	\$6.46	\$6.87	\$6.87
Total Bill:	\$67.94	\$72.34	\$72.34

#### *Finance Committee Recommendation*

Approve proposed wastewater rates for 2013 and 2014.

#### *Solid Waste*

The 2012 monthly solid waste rate for 35 Gallon Cart (weekly pick up) is \$19.71; the utility tax rate is 10.50%.

The Solid Waste Utility provides for the collection and disposal services that are provided to Kirkland residents and businesses by Waste Management Inc. (WMI), billing services performed by the utility billing division in Finance, and program development and outreach activities implemented by Public Works.

Approximately 90% of the City's total operating expenditures are payments made to other agencies. For instance, the King County Solid Waste Division (KCSWD) charges a tipping fee for disposal of solid waste hauled by WMI. The proposed 2013/2014 fee will increase 11.7% over the 2012 tipping fee. This will increase the fee from \$109/ton to \$121.75/ton and an increased cost to the Utility of approximately \$360,000 annually. The actual rate has not yet been adopted by the King County Council. In addition, the annual CPI increase to WMI in 2013 is 2.67% and is estimated to be 2.5% in 2014; an increase of approximately \$295,000.

Kirkland's direct costs to operate the utility account for the remaining 10% of the annual expenditures. Drivers of the 2013/2014 rate proposal include the following:

- The annual single family (SF) migration rate from larger carts to smaller carts is projected to be 5.6% in 2013 and 5.4% in 2014.

- A projected decrease in SF organics extras per month from 2,500 to 1,500 if the existing yard waste subsidy is eliminated.

Previously discussed with Council and the Finance Committee, significant elements of the current solid waste rate study/projections include:

- Shift from a fully linear rate model to one that is nearly linear (somewhat higher cost for smaller sizes)
- Charge per SF yard waste extra equal to WMI wholesale rate (estimate 1,500/mo)
- Charge per SF/commercial/multi-family garbage extra equal to WMI wholesale rate
- \$300,000 annual transfer to street preservation fund (impact of waste hauling on Kirkland streets)
- Retain cost split of organics program (SF 25% -- multi-family/commercial 75%)
- Retain cross-subsidization of SF and roll-off by commercial/MF that amounts to approximately \$390,000 and \$25,000 annually, respectively.
- Increasing the rate by the full amount necessary for the biennium in the 2013 and keeping it flat in 2014 rather than increase the rate in both 2013 and 2014.

Additional information regarding the proposed solid waste rates from Solid Waste Programs Lead, John MacGillivray is included as Attachment II.

Preliminary 2013-2014 rate increase:

Cart Size (Frequency)	# customers	2012 rate	One Year Implementation		
			\$ Increase	2013 Rate	2014 Rate
35 gal (monthly)	1,114	\$4.55	\$1.24	\$5.79	\$5.79
10 gal (weekly)	24	\$5.63	\$1.54	\$7.17	\$7.17
20 gal (weekly)	2,003	\$11.26	\$3.07	\$14.33	\$14.33
35 gal (weekly)	10,690	\$19.71	\$2.59	\$22.30	\$22.30
64 gal (weekly)	5,581	\$36.03	\$4.73	\$40.76	\$40.76
96 gal (weekly)	1,486	\$54.04	\$7.09	\$61.13	\$61.13

Resulting in a proposed single family monthly rate with utility tax included:

	2012	2013	2014
Typical Monthly Bill	\$19.71	\$22.30	\$22.30
Hazardous Waste	\$1.08	\$1.08	\$1.08
Utility Tax	\$2.07	\$2.34	\$2.34
Total Bill:	\$22.86	\$25.72	\$25.72

*Finance Committee Recommendation:* Approval of the proposed solid waste rates for 2013 and 2014. (NOTE: Kirkland is in the process of assessing fines against Waste Management for missed pickups during the strike. The amount collected may lower the overall rate increase.)

*Surface Water*

The 2012 monthly surface water rate is \$15.60 per single family dwelling; the utility tax rate is 7.5%.

The surface water utility provides for the construction, operation, and maintenance of surface water drainage courses, erosion control, water quality systems, and other program services such as outreach and citizen stewardship. The Utility enables the City to comply with Phase II of the National Pollutant Discharge Elimination System (NPDES) Municipal Storm water permit that is required by the Environmental Protection Agency's Clean Water Act. The Permit identifies a required level of system maintenance, monitoring, outreach, documentation, and other efforts that are intended to reduce flooding, control erosion, and, above all, protect water quality.

Annual capital and operational requirements for the Utility are based on the City's 2005 Surface Water Master Plan, and the proposed surface water rates for 2013/2014 also include an additional \$1 M per year for capital projects anticipated in the newly annexed JFK neighborhoods. \$950,000 per year is also transferred from the Utility to transportation capital projects to account for the surface water component of those projects; however, the average programmed surface water components that are identified in the 2013-2018 CIP are just \$378,000 per year – this is, among others, is being evaluated in the Master Plan update.

The Surface Water Master Plan update began in mid-2012; along with capital needs in the JFK neighborhoods, the appropriate level of depreciation funding for the system, and transportation needs, other City-wide surface water capital project needs are being reviewed. From 2012 to 2013 the surface water capital reserve balance will decrease from \$8.6 M to approximately \$5 M; this draw down is primarily due to the following:

- Use of \$1 M for the Cross Kirkland Corridor acquisition
- Use of \$3.3 M in 2013 for a significant Totem Lake culvert replacement

Additionally, for 2013, the proposed rate includes service package requests for:

- Dedicated TV inspection vehicle & crew of one each Senior Maintenance and Utility Worker (the existing TV inspection vehicle is shared with the wastewater division)
- Dedicated storm detention maintenance equipment of a mower, trailer, and pickup

These requests are related to annexation, are under evaluation and may be brought forward during the 2013/2014 budget process.

There is no increase recommended in the preliminary 2013-2014 surface water rates

	2012	2013	2014
Typical Monthly Bill	\$15.60	\$15.60	\$15.60
Utility Tax impact	\$1.17	\$1.17	\$1.17
Total Bill:	\$16.77	\$16.77	\$16.77

*Finance Committee Recommendation*

Approve proposed surface water rates for 2013 and 2014.

*Summary*

Typical Single Family Monthly Account

	2012	2013	2014
Water (7 units)	36.86	38.10	39.96
Sewer (6 units)	61.48	65.47	65.47
Solid Waste (35 Gallon)	19.71	22.30	22.30
Surface Water	15.60	15.60	15.60
Total	\$ 133.65	\$ 141.47	\$ 143.33
<i>\$ increase from previous yr</i>		<i>\$7.82</i>	<i>\$1.86</i>

Proposed Single Family Typical Monthly Rate with Utility Tax included:

	2012	2013	2014
Water (7 units)	41.79	43.20	45.30
Sewer (6 units)	67.94	72.34	72.34
Solid Waste (35 Gallon)*	22.86	25.72	25.72
Surface Water	16.77	16.77	16.77
Total	\$ 149.36	\$ 158.03	\$ 160.13
<i>\$ increase from previous yr</i>		<i>\$8.67</i>	<i>\$2.10</i>

\*includes \$1.08 per month Hazardous Waste fee

*(NOTE: Kirkland is in the process of assessing fines against Waste Management for missed garbage and recycling pickups during the strike. The fine amount collected may lower the overall solid waste rate increase.)*

*Next Steps*

September 4<sup>th</sup> – Rate presentation to Council  
September 18<sup>th</sup> – Rates to Council for adoption



**CITY OF KIRKLAND**  
Department of Finance & Administration  
123 Fifth Avenue, Kirkland, WA 98033 425.587.3100  
www.kirklandwa.gov

**MEMORANDUM**

**To:** Kurt Triplett, City Manager  
**From:** Tracey Dunlap, Director of Finance and Administration  
**Date:** July 5, 2012  
**Subject:** Utility Tax Accounting Change and Related Impacts

**RECOMMENDATION:**

Council receives briefing on changes to the City’s calculation of and accounting for City utility taxes and provides direction for inclusion in the 2013-2014 rate studies.

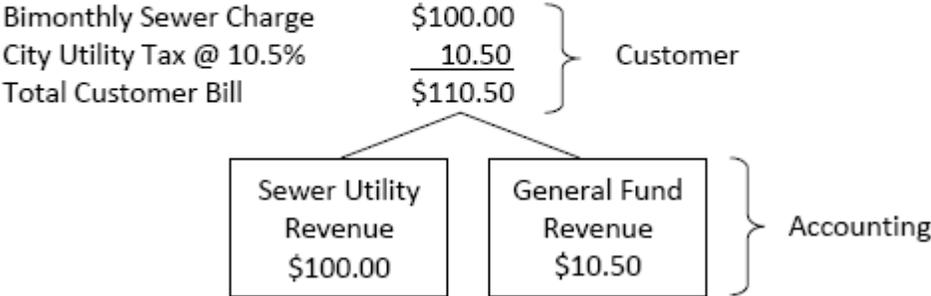
**BACKGROUND DISCUSSION:**

Historically, the City of Kirkland has charged and accounted for City utility taxes on the City-owned utilities (water, sewer, surface water, solid waste) in the following manner:

1. The customer charge is calculated based on the utility rate schedule.
2. City Utility tax is added to the bill as a separate line item.
3. Rate revenues are received to the appropriate utility enterprise fund
4. City Utility tax (City tax) revenues are received directly to the General Fund.

**Illustration 1**

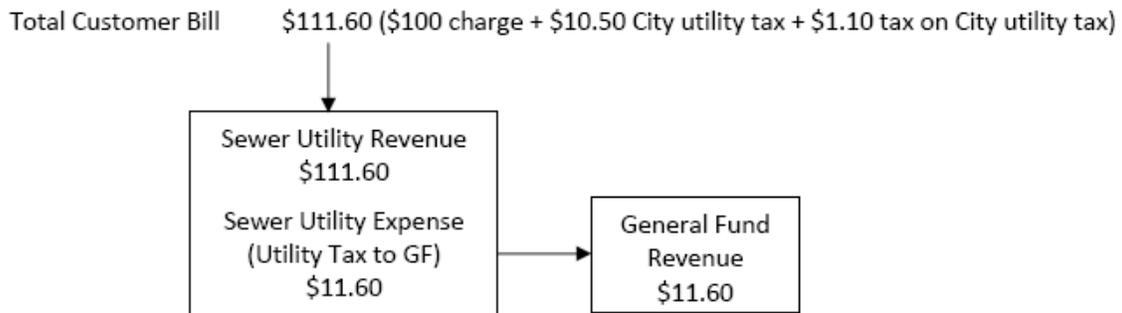
**Current Practice**



The State of Washington imposes a utility excise tax (State tax) on the “gross revenues” of the utilities and the City has historically paid this tax on the rate revenues received to the utilities, but not on the City tax. During the recent audit, DOR audited the City’s State tax payments and determined that the City should have been paying State taxes on both the rate revenues and the City utility taxes (see attached DOR Special Notice dated August 2011), which taken together should be treated as “gross revenues”. The State tax is typically built into utility rates.

Based on the recent interpretation, generally accepted accounting principles requires that the City account for the gross revenues in the utility funds, including the City utility taxes, which are then paid by the utility funds to the General Fund.

Illustration 2  
Revised Accounting Practice



This change has a number of consequences:

1. Increases the State taxes paid by the utilities, which will be taken into account during the rate updates for the 2013-2014 budget process.
2. Grosses up the budget by increasing the utility revenues and expenses by approximately \$4 million in City utility tax revenues added and \$4 million in expenditures for City utility tax payments to the General Fund. The General Fund budget would be unchanged in that the revenue would still be included but the amount could be larger (see below).
3. Changing the City utility tax calculation to be based on the “gross revenues” of the utility, which now includes the City utility tax, results in a “tax on a tax”. In reality, this is consistent with the fact that the City utility tax is a tax on the gross income of the utility, not on the customer. There are a few options for addressing this issue:

Option 1

Many utilities build the local and state utility taxes into the utility rates, since they are taxes on the utility (a cost of doing business). In some cases, the utility includes a note on the bill, such as “Rates include the impact of the City’s x.x% utility tax and the State’s y.y% utility excise tax”.

## Option 2

If it is desirable to continue to show the City utility tax as a line item on the bill, the tax rate would need to be grossed up to reflect the impact of applying the tax to the gross revenues. For example, 10.5% would effectively be  $10.5\% \times 10.5\% = 11.60\%$ . This would reflect the application of the tax to gross utility revenue and would increase City utility tax collections by at least \$500,000. PSE shows the total City tax as a line item on their bills titled "Effect of City Tax".

## Option 3

Lower the City utility tax rate, to neutralize the impact on utility tax revenues. For those utilities with 10.5% tax rate, the rate would be reduced to 9.58%.

An example of the options for a bimonthly sewer charge of \$100.00 follows:

	<b>Current</b>	<b>Option 1</b>	<b>Option 2</b>	<b>Option 3</b>
Utility Tax Rate	10.50%	10.50%	10.50%	9.58%
Sewer Charge	100.00		100.00	100.00
Effective Utility Tax	10.50		11.60	10.50
<b>Total Utility Bill</b>	<b>110.50</b>	<b>*111.60</b>	<b>111.60</b>	<b>110.50</b>

\*Note: Includes State Utility Excise Tax on collection at 3.852% and City Utility Tax on gross revenues at 10.5%

Staff has discussed these options with the Council Finance Committee and is recommending Option 3 for inclusion in the 2013-2014 rate updates.

An additional impact of the accounting change is the application of the tax rate to the gross revenues of the utilities, which subjects non-rate revenues to the tax. Since this is a tax on the utility, not on the customer, there are many instances where the added tax would be a significant burden and cannot be collected as an addition to the rate payers. A few examples include the Regional Capital Facilities Charges (RCFCs) which are remitted to Cascade Water Alliance (CWA) for new water connections, City capital facilities charges for new connections, interest earnings and grants. As a result, staff is recommending that the KMC be revised to exclude selected revenues from the gross revenues definition, specifically:

- Interest revenue,
- Capital facilities charges (including RCFCs and Emergency Sewer Program connection revenue),
- Grant revenue,
- Intergovernmental revenue (cost reimbursements from other jurisdictions), and
- Interfund transfers (cost reimbursements for work for other City funds).

Staff is seeking direction regarding the inclusion of Option 3 in the rate analysis and the recommended changes to the KMC.



# Special Notice

WASHINGTON STATE DEPARTMENT OF REVENUE

AUGUST 15, 2011

## City-imposed Municipal Utility Taxes are Part of Taxable Gross Income

### Background

In some cases, cities provide utility services directly to their citizens. Many cities also impose a municipal utility tax on the **providers** of certain utility services. The municipal utility tax also applies to a department of the city that provides utility services.

If a city itself operates a department that provides utility services directly to its citizens, the municipal utility tax also applies to those services. The municipal utility tax is then passed on to and collected from customers by the utility provider. In some cases the municipal utility tax may be separately identified on the billing invoice to show the “effect” of the tax.

### How do I report?

The entire amount charged to and collected from customers is gross revenue to the utility provider. This amount cannot be reduced by the amount of recovered taxes when the utility provider computes its state public utility tax or business and occupation tax liability, even if the city itself provides the utility service.

### Example

City Z imposes a public utility tax on providers of water distribution services within its city limits. City Z’s Water Department provides water services to residents of City Z. City Z’s Water Department is subject to City Z’s utility tax. City Z’s Water Department passes on the local utility tax to its customers.

The entire amount that City Z’s Water Department bills to its customers for water services, including the municipal utility tax liability (even if separately stated on the billing invoice), is subject to the state public utility tax under the water distribution classification.

### For more information

Visit our website at [dor.wa.gov](http://dor.wa.gov), send an email to [dorcommunications@dor.wa.gov](mailto:dorcommunications@dor.wa.gov), or call the Department’s Telephone Information Center at 1-800-647-7706.



**CITY OF KIRKLAND**  
Department of Public Works  
123 Fifth Avenue, Kirkland, WA 98033 425.587.3800  
[www.kirklandwa.gov](http://www.kirklandwa.gov)

---

## MEMORANDUM

**To:** Kurt Triplett, City Manager

**From:** John MacGillivray, Solid Waste Programs Lead  
Ray Steiger, P.E., Public Works Director

**Date:** August 27, 2012

**Subject:** 2013/2014 Solid Waste Rates

### **RECOMMENDATION:**

Staff recommends that the City Council receive a presentation on the proposed 2013/2014 Solid Waste rates. Staff recommends a 13.39% average overall rate increase and recommends that the rate increase be implemented all in the first year of the two year rate.

### **BACKGROUND DISCUSSION:**

At its February 28, 2012 meeting, the Finance Committee received a briefing on the circumstances that caused the revenue deficit in the 2012 solid waste rates. At the March 27, 2012, Finance Committee meeting, staff introduced several potential rate options intended to correct the revenue deficit in the 2013/2014 solid waste rates. The Finance Committee subsequently indicated an interest in further discussion of the linear and "nearly" linear rate options. Accordingly, a refined list of three rates options were presented for the Finance Committee's review and consideration at the May 29, 2012, meeting. At that meeting, staff received unanimous direction from the Finance Committee to:

- 1) Develop the 2013/14 solid waste rate model in accordance with the nearly Linear 1 option;
- 2) Remove the 100% subsidy of yard waste extras in the proposed solid waste rates; and
- 3) Remove the partial subsidy of garbage extras in the proposed solid waste rates.

### *Public Safety Committee Meeting Summary*

At the July 17 City Council Study Session, staff presented details of the solid waste rates policy review process and the aforementioned Finance Committee's 2013-2014 solid waste rate policy recommendations. At that session, Councilmembers had some questions and comments concerning the proposed revisions to the City's solid waste rates policy. The staff responses to those questions and comments are included in the attached August 15 memorandum to the Public Safety Committee (*Attachment 1*). A summary of the feedback received from the Public Safety Committee is highlighted in red below each question.

## PROPOSED 2013/2014 SOLID WASTE RATES

*Attachment A, 2013/2014 Solid Waste Rates Increase Reconciliation Table* is offered as a tool to illustrate and simplify the individual elements of the proposed solid waste rates. *Attachment B, Proposed 2013/2014 Solid Waste Rates Comparison Table* is included to show the percentage increases and cost for each cart size under the one year and two year rate increase implementation scenarios.

Staff recommends that the 13.39% rate increase be implemented all in the first year of the two year rate. In both the one and two year rate increase implementation scenarios, the overall revenue requirement over the course of the two years is the same, and the amount of revenue collected from rate payers will be the same at the end of the two year cycle. The difference between the one and two year scenarios is that in the one year scenario the rate increase is implemented all in the first year and provides a sufficient reserve in the Utility – the reserve draws down significantly with a two year phase in approach.

In the two year scenario, a portion of the increase needed to cover first year costs is deferred until the second year. This makes it necessary to collect extra revenue in the second year to cover the first year deficit. Consequently, if a two year rate implementation is selected, the cash balance in the Solid Waste Utility will be drawn down to between \$310,000 and \$546,000 at the end of 2013. Since the City bills its customers bi-monthly but pays Waste Management monthly, it has been past practice to maintain a cash balance greater than or equal to one month's payment to Waste Management for collection and disposal (typically approximately \$950,000/month). The estimated ranges of the cash balance related to each implementation scenarios may be found at the bottom of *Attachment A*.

### *Rate Design and Components*

Per the direction of the Finance Committee and in accordance with the Nearly Linear 1 rate structure, the rates for the smaller cart sizes (35 gallon monthly and 10 and 20 gallon weekly) were increased more than the larger cart sizes (35, 64, and 96 gallon weekly) in order to create a \$50,000 annual reserve to hedge against unanticipated downsizing. The move to the Nearly Linear rate structure is made as a means through which to somewhat reduce the risk of a revenue shortfall as a result of residential customers choosing to downsize (migrate) from larger to smaller cart sizes.

The relative increase of the smaller to the larger carts is approximately 27.3% versus 13.1% in the recommended one year implementation scenario. In terms of a relative cost per gallon, the price of the smaller carts is 72 cents per gallon versus 64 cents per gallon for the larger carts. In a full linear model, the cost per gallon is the same across all cart sizes; however, while there is a slight difference in price per gallon between the smaller and larger carts in the Nearly Linear rate model which makes the larger carts a nominally "better deal", this difference is relatively small and consequently still strongly encourages downsizing and positive waste reduction and recycling behaviors that support the environmental goals of the City Council.

The proposed rates also remove all subsidies for yard waste and garbage extras and, if adopted, customers will be billed the wholesale rate paid to Waste Management plus state taxes to fully cover Utility costs for each 32 gallon equivalent unit of yard waste and garbage (\$5.07). If the 100% subsidy of yard waste extras was to remain in the proposed rates, the

overall rate increase would be 13.94% for the recommended one year implementation and 9.02% for both 2013 and 2014 under the two year implementation.

### *Solid Waste Rate Increase Components*

Most of the proposed rate increase can be attributed to four factors:

Post-annexation downsizing: Migration from larger to smaller collection cart sizes among residential customers following annexation was higher than anticipated, and is expected to average 5.7% in 2012. Due to revenue being less than costs for the smaller cart sizes, and vice versa for the larger carts, this unanticipated residential cart downsizing causes a projected imbalance between revenues and costs in 2012. There were also unanticipated changes in multifamily, commercial, and roll-off service level choices that are negatively impacting the revenue-cost balance in 2012. As a result there are increased annual net costs of approximately \$450,000 that need to be covered by raising rates in 2013.

Tipping Fee Increase: The tipping fee (disposal fee) paid to the King County Solid Waste Division (KCSWD) is proposed to increase from \$109/ton to \$121.75/ton in 2013/2014. This is an 11.7% increase over the 2012 tipping fee and contributes 3.1 percentage points (pp) to the proposed rate increase. This increases costs by approximately \$360,000. The majority of the increase can be attributed in part to a decline in tonnage received at the Cedar Hills Landfill, debt service on short term bonds to fund the transfer station improvements, grant programs, and an increase in the Landfill Reserve Fund.

CPI Increase to Waste Management: The CPI increase for June 2012 versus June 2011 is 2.67%. The CPI increase for June 2013 compared with June 2012 is assumed to be 2.5%. These CPI increases require an increase in rate revenue of approximately \$295,000.

Projected Residential Downsizing in 2013/2014: Annual residential customer downsizing in 2013 and 2014 is projected to be slightly less than in 2012; however, downsizing is still projected to average nearly 5.5%. Compensating for this continued migration requires an increase in rate revenue of about \$170,000. It is assumed that service level choices by multifamily, commercial, and roll-off customers in 2013 and 2014 will not affect the revenues versus costs balance in 2013 and 2014.

### *Distribution of Rates Among Sectors*

The proposed 13.39% increase is a combined average of the increase for each sector. The required rate increases for the single family, multifamily/commercial, and roll-off sectors are different as shown at the bottom of *Attachment A*. Rate increases for the 2013/2014 period for each sector are different due to factors that affect Kirkland solid waste collection customers differently. The most important factors include:

1. Disposal and collection costs – Drop box and large compactor customers pay solid waste rates that exclude disposal costs. Multifamily and commercial customers pay rates that reflect approximately a 50/50 split between disposal costs and collection costs. Single family residential customers pay rates that reflect a 20/80 split between disposal and collection costs. Consequently, the relative rate increase for the single family sector is the highest and the relative rate increase for the roll-off sector is the lowest.

2. *Migration* – Most of the migration since annexation and projected through 2014 is the result of downsizing by single family residential customers.
3. *Organics extras* – Single family residential customers produce the organics extras that are currently picked up at no charge to these customers whereas multifamily and commercial produce almost no organics extras.
4. The rates for smaller single family residential garbage cart sizes are non-linear.

In addition, multifamily/commercial customers currently pay rates that raise approximately \$405,000 more than the costs incurred for these customers. This revenue surplus subsidizes single family residential customers by approximately \$380,000 and roll-off (drop box and large compactor) customers by approximately \$25,000 – that is, these customers pay rates that do not fully cover the costs incurred to manage their solid waste.

If cross subsidies are maintained at their current levels, then the 13.39% average one year rate increase would be allocated to the three customer classes such that residential customers rates will go up approximately 15.5%, multifamily/commercial rates will go up 11%, and roll-off rates up approximately 9%. The differential rate increases are due to the differential impacts of changes in disposal and collection costs, downsizing, organics extras charges, and non-linear rates. It should also be noted that maintaining the current level of cross subsidies means that the \$50,000 surplus for hedging against unanticipated downsizing in 2013/2014 will in effect be provided by multifamily/commercial customers, rather than the residential customers with non-linear rates.

Hence, there is a *policy choice* between allocating rate increases based on what customers cause which cost increases that would tend to maintain current cross-subsidization levels, or increasing rates for all customers equally; this would result in an increase in cross subsidization of single family residential customers by multifamily/commercial customers. The subsidization of roll-off by multifamily/commercial would be reduced because the tip fee increase would be applied to roll-off haul rates.

#### *Other Considerations*

City staff is currently in the process of determining the potential performance fees which may be assessed to Waste Management due the garbage and recycling driver strike that occurred between July 25 and August 1. The penalties collected may be substantial, and the options for use of the funds could include issuing a credit to customers for a week's worth of missed service, replenishing the Solid Waste Utility cash reserve, and/or using the fees to mitigate future solid waste rate increases.

#### PROPOSED SOLID WASTE RATES SUMMARY

Staff recommends that the proposed 2013/14 Solid Waste rates include the following components:

- A 13.39% overall average rate increase. The average rate increases by sector are:
  - 15.58% to Single Family Residential customers
  - 10.84% to Multifamily Residential and Commercial customers
  - 9.22% to Roll-off Customers

- A shift from a fully linear rate model to a nearly linear rate model. The rates for residential customers with smaller carts (35 gal/monthly and 10 and 20 gal/weekly) would be increased by 27.3% and the rates for residential customers with larger carts (35, 64, and 96 gal weekly) would be increased by 13.1%.
- Extra rates collected (\$50,000/year) to hedge against unpredicted downsizing.
- Included \$300,000 street preservation allocation
- The elimination of the 100% subsidy of yard waste extras. The proposed charge per yard waste extra (32 gallon equivalent) is \$5.07/each. For 2012, the City pays Waste Management \$4.71 per extra but receives no compensatory revenue.
- The elimination of the partial subsidy of garbage extras. The proposed charge per garbage extra (32 gallon equivalent) is \$5.74/each. In 2012, the City pays Waste Management \$5.24 per extra but receives only \$4.16 per extra in compensatory revenue.

NEXT STEPS

Month/Date	Task	Status
Jan	Rates Study Consultant Procurement	Complete
Feb/Mar/Apr/May	Finance Committee Rates Policy Review	Complete
May	Data Gathering/Admin Budget Review	Complete
June	Conduct Rate Study	Complete
July	Internal Review	Complete
August 15	Public Safety Committee Rate Policy Review	Complete
August 20	Finance Committee	Complete
September 4	City Council Meeting Utility Rates Review	Pending
September 18	City Council Meeting Rates Ordinance Adoption	Pending
October 15	Deadline to pass rates ordinance	Pending



**CITY OF KIRKLAND**  
Department of Public Works  
123 Fifth Avenue, Kirkland, WA 98033 425.587.3800  
[www.kirklandwa.gov](http://www.kirklandwa.gov)

---

## MEMORANDUM

**To:** City Council Public Safety Committee

**From:** John MacGillivray, Solid Waste Programs Lead  
Ray Steiger, P.E., Public Works Director

**Date:** August 15, 2012

**Subject:** 2013/2014 Solid Waste Rates

### **STAFF RECOMMENDATION**

Staff recommends that the City Council Public Safety Subcommittee receive a brief presentation on the proposed 2013/2014 Solid Waste rates policy to answer questions posed and comments made by the City Council at its July 17 Study Session.

### **BACKGROUND**

At its February 28, 2012 meeting, the Finance Committee received a briefing on the circumstances that caused the revenue deficit in the 2012 solid waste rates. At the March 27, 2012 Finance Committee meeting, staff introduced several potential rate options intended to correct the revenue deficit in the 2013/2014 solid waste rates. The Finance Committee subsequently indicated an interest in further discussion of the linear and "nearly" linear rate options. Accordingly, a refined list of three rates options were presented for the Finance Committee's review and consideration at the May 29, 2012 meeting. At that meeting, staff received unanimous direction from the Finance Committee to:

- 1) Develop the 2013/14 solid waste rate model in accordance with the nearly linear option;
- 2) Remove the 100% subsidy of yard waste extras in the proposed solid waste rates; and
- 3) Remove the partial subsidy of garbage extras in the proposed solid waste rates.

### **STUDY SESSION FOLLOW-UP**

At the July 17 City Council Study Session, staff presented details of the solid waste rates policy review process and the aforementioned Finance Committee's 2013-2014 solid waste rate policy recommendations. Councilmembers had some questions and comments concerning the proposed revisions to the City's solid waste rates policy:

**1) Attention should be given to reducing the disposal fees (tipping fees) paid to the King County Solid Waste Division (KCSWD).**

The KCSWD originally proposed a 14.7% increase in its tipping fee from \$109/ton to \$125/ton for the 2013/2014 biennium. Based upon feedback from several King County cities, including Kirkland, the KCSWD revised its proposed rate to \$121.75/ton. As noted in *Attachment A*, the KCSWD made several reductions to its proposed rate including deferring the purchase of the property for the Northeast King County Transfer Station; reducing the cash contribution to its capital improvement program; deferring the implementation of the new Zero Waste of Resources Grant; and several other adjustments such as deferring studies, surveys, and some operations and maintenance projects.

**Public Safety Committee Feedback: None received.**

**2) What effects will eliminating the 100% subsidy of residential yard waste extras have on the City's recycling diversion rate?**

At the July 17, 2012 City Council study session, staff was asked to determine how eliminating the subsidy on residential yard waste extras would impact the City's recycling diversion rate. Staff polled solid waste experts at several cities including Bothell, Bellevue, Renton, Federal Way, and Auburn and the KCSWD in search of data which would help predict the impact. The cities polled and the KCSWD were not able to offer any hard data which would allow staff to accurately predict any potential negative effects on the diversion rate. The experts did offer the following observations:

- Roughly the same amount of organic waste will be collected but customers are likely to adjust their behavior and mete out their yard waste over the course of a growing season rather than regularly putting out numerous extras all at once.
- For the typical customer/homeowner, a 96-gallon yard waste cart is a reasonable amount of capacity to be embedded in the garbage rate and provided at no additional cost.
- Curbside collection of organics will continue to be the most popular form of disposal. Organics are banned from the landfill and not accepted at transfer stations. This leaves backyard composting or illegal dumping as the only alternatives. The communities polled indicated that charging for yard waste extras did not cause any significant issues with illegal dumping of yard waste.

Based upon the staff experience and the comments received, staff does not anticipate that eliminating the residential yard waste extras subsidy will have any significant negative impact upon the City's single family residential recycling diversion rate. Elimination of the yard waste extras subsidy will save the Utility approximately \$150K per year.

**Public Safety Committee Feedback:** Removing the yard waste extra subsidy from the rates appears to be primarily an economic decision and more consideration should be given to the environmental impacts of ending the subsidy. The impact of keeping the yard waste extras in the rates (.50 of a percentage point) is relatively inconsequential in light of the overall large rate increase of about 13%. Charging customers could also result in an increase in illegal dumping activity.

**3) The current linear rate structure provides the most incentive to reduce waste and recycle more. Why is a shift to a nearly linear solid waste rate structure preferred over maintaining the status quo?**

Kirkland's residential rates are currently linear. That is, each cart size and collection frequency shares in total costs in proportion to its share of total monthly collection container capacity for all residential service levels. For example, Kirkland now charges its customers a flat, linear rate of about 56¢ per gallon for each of its six residential cart service levels. Under the residential rate option of maintaining current linear rates any increase in total costs for residential collection and disposal would be passed on with equal percentage increases for all cart sizes and collection frequencies. For example, if residential costs go up by 10% in 2013 then all residential rates would go up 10%.

Under the full linear rate structure, the City pays Waste Management more than it receives in revenue for the smaller cart sizes and receives more revenue than it pays to Waste Management for the larger cart sizes. In effect, the revenues received from the larger cart sizes subsidize the costs of the smaller cart sizes.

While full linear rates offer the most diversion and waste prevention benefit, its revenue component is the most sensitive to fluctuations in service levels (downsizing). If downsizing levels can be accurately predicted, however, then staying linear is the preferred option. Since annexation, the rate of downsizing has leveled off to approximately 0.63% per month which is equivalent to the migration rate in pre-annexation Kirkland. Before annexation, the migration rate from the 96/64 weekly carts to the smaller 35 monthly and 10, 20, and 35 weekly carts was about 0.60% per month. However, if an unpredicted spike in downsizing occurred due to a successful education and outreach effort promoting the City's variable rates or a further slump in the economy, for example, expenditures would likely outpace revenues further depleting the Utility's limited cash reserves.

The recommended move away from the fully linear rate structure to the nearly linear rate structure is made as a means through which to somewhat reduce the risk of a revenue shortfall as a result of customers downsizing from larger to smaller carts. In many ways, we are victims of our own success; the linear rates have been overwhelmingly effective at driving more and more customers to the smaller, cheaper cart sizes where the Utility is losing money.

The nearly linear option increases the prices of the smaller carts sizes (35 gallon monthly and 10 and 20 gallon weekly) to slightly increase revenue as a hedge against unanticipated downsizing. The cushion built into the current rate model is approximately \$50K/year. Consequently, the nearly linear structure does result in a considerably larger percentage rate increase for the smaller 10W, 20W, and 35M service levels compared to

the larger 35W, 64W, and 96W service levels. Yet, in terms of actual dollars, the increase is relatively small by comparison; for example, a hypothetical 30% increase in the 20 gallon service increases the price by \$2.36 to \$14.75/month and a 10% increase in the 96 gallon service increases the price by \$5.40 to \$59.44/month.

While the nearly linear alternative insulates the Utility from some of the revenue risk caused by ongoing downsizing, it still strongly encourages the same recycling diversion and waste prevention behaviors intrinsic to the fully linear rate structure.

**Public Safety Committee Feedback:** The proposed move from linear to nearly linear might be an overreaction to the hyper downsizing which occurred after annexation given that the rate of downsizing has appeared to return to pre-annexation levels. The rate policy change appears to be driven only by economics and more consideration should be given to the potential environmental detrimental effects of moving away from linear. The nearly linear model provides customers with less of an incentive to downsize and reduce their waste since the cost per gallon for the smaller cart sizes is slightly higher than the cost per gallon for the larger carts sizes. Members expressed an interest in seeing if the prices of the individual carts in the nearly linear model could be distributed in a fashion that would still encourage downsizing but still meet the Utilities revenue requirements.

#### **NEXT STEPS**

After receiving input from the Public Safety Committee, staff will present the final proposed 2013/2013 Solid Waste rates to the City Council Finance Committee on August 20. At the September 4 City Council meeting, staff will bring forward it utility rate recommendations for the Council's review and consideration. At the September 18, the utility rates will be proposed for adoption by the Council.

**ATTACHMENT A: 2013/2014 Solid Waste Rates Increase Reconciliation Table**

Rate Element	One Year Rate Increase		Notes
	Rate Impact in Percentage Points		
	2013	2014	
Downsizing Through May 2012	3.89 (29.1%)		Unanticipated post-annexation downsizing through May 2012 (~\$426K)
King County Tipping Fee	3.13 (23.4%)		11.7% increase from \$109/ton to \$121.75/ton
CPI Increase to WMI	2.57 (19.2%)		100% of June CPI increase to Waste Management
Projected Downsizing 2013/2014	1.54 (11.5%)		Projected downsizing in 2013 and 2014 (5.6% in 2013 and 5.4% in 2014)
Administration/Billing	0.90 (6.7%)		Compensation and increased internal service costs
Yard Waste Extras	0.79 (5.9%)		Payment to WM for an estimated 1,500 extras
Non-Linear Rates	0.44 (3.3%)		Non-linear rates for 35M, 10W, and 20W single family service levels
State Excise Tax	0.30 (2.2%)		State tax on City tax
Increased Charge for Refuse Extras	0.07 (<1%)		End partial subsidy of garbage extras
Increased Commercial Organics Customers	0.03 (<1%)		Small increase in number of participants in Commercial Organics Program (100% subsidized in rates)
Anticipated B & O Tax Decrease	-0.27 (-2.0%)		Projected reduction in B&O tax from 1.8% to 1.5% in mid-2013
Deferral of 2013 Rate Increase to 2014			
2014 Rate Increase to Offset 2013 Deficit			
Overall Average Rate Increase	13.39%		Combined average rate increase for single family, multifamily/commercial, and roll-off services
Single Family	15.58%		Rate increase by sector
Multifamily/Commercial	10.84%		Rate increase by sector
Roll-Off	9.22%		Rate increase by sector
Projected Cash Balance	\$815K - \$1.05m	\$683K - \$919K	Projected range of Solid Waste Utility cash balance by year