

**Council Meeting: February 15, 2011****SUBJECT: Agreement on Stranded Assets and Extension of Term, Refuse Collection Franchise Agreement****REPORT IN BRIEF**

Bay Counties Waste Services (BCWS), the City's franchised refuse and recycling collection contractor, has identified "stranded assets" as a potential barrier to borrowing the capital it needs to provide services required by its contract with the City. The contract, which is adopted in the form of an ordinance, requires BCWS to purchase trucks and other equipment that have lives that are longer than the contract under which BCWS is reimbursed by the City.

After discussing various alternative solutions with BCWS, staff is recommending that Council introduce an ordinance (Attachment A) and authorize the City Manager to execute an amendment to the franchise agreement that:

- Extends the term of the Agreement by three years, to June 30, 2021.
- Makes mandatory the City's current option to take ownership of BCWS's assets at the end of the term. If a Request for Proposals (RFP) is used to select the service provider beyond the end of the franchise term, that RFP would require that the incoming contractor purchase the assets from the City for the same price paid by the City. If BCWS were to continue providing services under a new franchise agreement, the assets would remain with BCWS.
- Tasks the City and BCWS to work cooperatively through the remainder of the extended term to adjust asset purchase timing so as to minimize the City's financial obligation at the end of the term.
- Corrects minor typographical errors in the current franchise agreement.
- Caps an existing incentive payment, resulting in an immediate, then ongoing savings to the City of \$93,853 per year.
- Documents the company's reduction of commercial refuse collection routes from ten to nine, resulting in annual savings of \$222,000.
- Requires BCWS to reduce the number of residential refuse routes from nine to eight, resulting in annual savings of \$225,000 per year.

Total ongoing savings as a result of the final three items listed is estimated to total approximately \$540,000 per year. These savings will be incorporated into the long range financial plan to the benefit of the City's refuse collection rate payers.

BACKGROUND

BCWS provides refuse and recycling collection services to the City under an exclusive franchise agreement. The term of the agreement ends June 30, 2018. BCWS receives an annual “contractor payment” from the City that is based on its allowable costs and includes a profit based on a percentage of those costs. The contractor payment is incorporated into the refuse collection charges billed to Sunnyvale residents and businesses, and is the largest single component of those charges.

One of the allowable costs is BCWS’s cost to purchase trucks, bins, boxes, carts and other depreciable assets used to provide services. BCWS is compensated by dividing the purchase price of each asset by the number of years over which it is depreciated. That amount is then paid to the company during each year of the asset’s life. For example, for a collection truck costing \$350,000 and having a life of 10 years, the company would receive \$35,000 each year for 10 years, plus \$3,251 in profit.

EXISTING POLICY

Solid Waste Sub-Element

Goal 3.2A Ensure that all municipal solid waste generated within the City is collected and transported in a manner that protects public health and safety.

Policy 3.2A.1 Provide convenient, competitively priced solid waste collection services

Goal 3.2G Contribute to an economic development environment that is supportive of a wide variety of businesses.

Policy 3.2G.1 Provide solid waste services desired by businesses at competitive rates

DISCUSSION

BCWS has made the City aware of the company’s concerns regarding its potentially “stranded assets.” Stranded assets is a reference to trucks and other equipment that BCWS must purchase in order to provide services required by the franchise agreement but whose cost will not be fully recovered by the company by the end of the franchise term.

This issue was discussed by the City and BCWS in the process of negotiating the language of the Extended and Second Restated Franchise Agreement that was approved by Council on December 14, 2004 (RTC 04-436). Section 11.03B of the Agreement gave the City the right, but not the obligation, to take ownership of all of the BCWS assets at the end of the term by paying the company the total unrecovered value of the assets.

BCWS is now beginning to purchase trucks with ten-year lives whose cost will not be fully recovered by the end of the franchise in 2018. A particularly large truck purchase is scheduled in Fiscal Year 2011/12 as the 16 collection vehicles purchased in 2001/02 reach the ends of their 10-year lives. The company reports that its lender is reluctant to extend credit in this situation since it has no assurance that the City will exercise its right to purchase the assets if the franchise ends in 2018 (as contemplated by the Agreement) and BCWS is not awarded a new or extended franchise at that time. BCWS points to the tighter underwriting standards following the 2008 banking crash as an explanation why the 2004 contract language no longer satisfies lenders.

Discussions between City staff and BCWS have resulted in a comprehensive solution to the stranded assets issue, as described in the proposed "First Amendment to Extended and Second Restated Agreement Between the City of Sunnyvale and Bay Counties Waste Services, Inc. For Solid Waste Collection and Recycling" (the Amendment), shown as Attachment B.

The Amendment makes the following changes to the Franchise Agreement:

- Extends the term of the Agreement by three years, to June 30, 2021¹. In doing so, it assures recovery by BCWS and its lender of the vast majority of the cost of the large truck purchase in 2011/12.
- Makes mandatory the City's current Section 11.02B option to take ownership of BCWS's assets at the end of the term. Handled correctly, this would see the City taking ownership of the assets for as little as one day. If an RFP is used to select the service provider beyond the end of the franchise term, that RFP would require that the incoming contractor purchase the assets from the City for the same price paid by the City. If BCWS were to continue providing services under a new or extended franchise agreement, the assets would remain with BCWS.
- The City and BCWS will work cooperatively through the remainder of the extended term to adjust asset purchase timing so as to minimize the City's financial obligation at the end of the term. At the present time the City obligation is projected to be \$6-8 million.
- Corrects minor typographical errors (Items 7-10) in the 2004 document.

These changes eliminate BCWS's exposure to stranded assets issues, which should no longer be an issue with regard to the franchise agreement.

¹ It is not possible to extend the franchise beyond June 30, 2021, as the term of the franchise began on July 1, 1991 and the City Charter limits franchises to a maximum of 30 years. For example, the original refuse collection franchise, issued to Specialty Garbage in 1960, expired in 1990. Prior to that date a Request for Proposals process was used to select a franchised hauler for a new franchise. A separate, one-year interim agreement with Specialty Garbage bridged the year between 1990 and the start of the current franchise in 1991.

Other changes included in the amendment will reduce BCWS's operating costs and will provide the City long term reductions in the amount of the contractor payment. These items are due to a combination of increased efficiency in BCWS operations, a reduction over the last 10 years in the quantity of commercial garbage and a shift of residential discards from garbage carts to yard waste and recycling carts (likely due to the financial incentives provided by the ChoiceCollect changes introduced to residents in 2008). The cost reductions include:

- An ongoing reduction in the Residential Refuse Collection Incentive payment currently paid to BCWS. This will reduce the current (FY 2010/11) contractor payment by \$93,853 and reduce future payments by a similar amount.
- Documentation of the company's already-implemented reduction of commercial refuse collection routes from ten to nine, effective September 1, 2010. This change will result in an ongoing cost savings estimated at \$222,000 per year.
- Following execution of this Amendment, BCWS will reduce the number of residential refuse routes from nine to eight. This change will result in an ongoing cost savings estimated at \$225,000 per year.

When fully realized in Fiscal Year 2013/14, annual operating savings will total approximately \$540,000.

FISCAL IMPACT

Depending on the type of cost, some changes to Specialty costs are reflected in the contractor payment sooner than others. The changes to the City's cost over time are estimated as follows, stated in 2010 dollars.

	FY 2010/11 (current year)	FY 2011/12 (estimate)	FY 2012/13 (estimate)	FY 2013/14 and thereafter (estimate)
Savings to City	\$135,627	\$245,000	\$426,000	\$540,000

Of the \$135,627 savings in the current year, \$41,774 is already captured in the current contractor payment amount (savings from cancellation of a planned commercial collection truck purchase). The remaining \$93,853 will be deducted from the current year's contractor payment prior to the end of the fiscal year.

The contractor payment to BCWS is the single biggest expense in the Solid Waste Management Fund. The Fiscal Year 2010/11 budget projects a 7% increase in solid waste rates for 2011/12 and a 3% increase for both 2012/13 and 2013/14. The savings from this action are equal to approximately half a percent of the total revenue requirement for Fiscal Year 2011/12 and about

1.3% of the total revenue requirement for Fiscal Year 2013/14 (when savings reach their maximum amount), meaning that all other things remaining constant, the rate increases could be reduced by those amounts in their respective years. However, the weak economy and the corresponding drop in solid waste business activity have resulted in a drawdown of reserves in the Solid Waste Management Fund over the last several years. As part of the FY 2011/12 rate setting process, staff will integrate the savings into the Solid Waste Rates in a way that will maximize the rate benefits while maintaining the sound fiscal position of the solid waste management fund.

PUBLIC CONTACT

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's Web site.

ALTERNATIVES

1. Introduce an ordinance adopting the First Amendment to Extended and Second Restated Agreement Between the City of Sunnyvale and Bay Counties Waste Services, Inc. For Solid Waste Collection and Recycling and authorize the City Manager to execute the amendment.
2. Take no action and allow the franchise agreement in its present form to remain in force.

RECOMMENDATION

Staff recommends Alternative No. 1: Introduce an ordinance adopting the First Amendment to Extended and Second Restated Agreement between the City of Sunnyvale and Bay Counties Waste Services, Inc. For Solid Waste Collection and Recycling and authorize the City Manager to execute the amendment.

Amending the franchise agreement as described will, at no cost to the City, remove a barrier to BCWS obtaining the capital it needs to provide services required by the franchise agreement. The amendment also provides significant long term cost savings to the City's refuse collection rate payers.

Reviewed by:

Marvin Rose, Director, Department of Public Works
Prepared by: Mark Bowers, Solid Waste Program Manager

Reviewed by:

Grace Leung, Finance Director

Approved by:

Gary M. Luebbers
City Manager

Attachments

- A: Draft Ordinance
- B: First Amendment to Extended and Second Restated Agreement Between City of Sunnyvale and Bay Counties Waste Services, Inc. For Solid Waste Collection and Recycling

ORDINANCE NO. _____

**AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF
SUNNYVALE ADOPTING THE FIRST AMENDMENT TO EXTENDED
AND SECOND RESTATED AGREEMENT BETWEEN THE CITY OF
SUNNYVALE AND WITH BAY COUNTIES WASTE SERVICES, INC.
FOR THE COLLECTION OF SOLID WASTE AND RECYCLING**

WHEREAS, Bay Counties Waste Services, Inc. (formerly named Specialty Solid Waste & Recycling, Inc.) entered into a Franchise Agreement with the City of Sunnyvale for the collection of solid waste in 1990, for a term of ten years, to run July 1, 1991 through June 30, 2001; and

WHEREAS, the Franchise Agreement subsequently was amended a number of times, which resulted in an extension of the term of the agreement to a 20 year period, to expire on June 30, 2011, and these amendments were incorporated into an overall restated franchise agreement adopted by ordinance no. 2572-97; and

WHEREAS, on November 11, 2003, the City Council adopted Ordinance 2771-04 extending the term of the Franchise Agreement for a total of 27 years, to expire on June 30, 2018, upon certain conditions; and

WHEREAS, Bay Counties Waste Services, Inc. raised issues regarding potentially "stranded assets" in reference to trucks and other equipment they must purchase to provide services as required under the Franchise Agreement which could prevent financing the equipment; and

WHEREAS, the City and Bay Counties entered into good-faith negotiations to address the stranded-asset issue; and

WHEREAS, the City and Bay Counties Waste Services, Inc. have negotiated an updated and amended Franchise Agreement to address those issues, including extending the term of the Franchise Agreement by three years with an expiration date of June 30, 2021, making mandatory the purchase of assets at the end of the franchise term, work cooperatively to adjust asset purchase timing, capping an incentive payment resulting in ongoing savings to the City, reducing the commercial and residential routes with resulting annual savings; and

WHEREAS, the amended franchise agreement is in the best interest of the City and ratepayers; and

WHEREAS, Article XVI of the Charter of the City of Sunnyvale, concerning franchises, provides that substantive grants, renewals and amendments of franchises be done by ordinance.

NOW, THEREFORE, THE CITY COUNCIL OF THE CITY OF SUNNYVALE DOES ORDAIN AS FOLLOWS:

SECTION 1. FRANCHISE AGREEMENT AMENDED. The Council hereby approves and incorporates by reference the First Amendment to Extended and Second Restated Agreement Between the City of Sunnyvale and Bay Counties Waste Services, Inc. for Solid Waste Collection and Recycling as set forth in Exhibit A attached hereto, which includes extending the term of the franchise agreement by three years with an expiration date of June 30, 2021; making mandatory the

purchase of assets at the end of the franchise term; working cooperatively to adjust asset purchase timing, capping an incentive payment resulting in ongoing savings to the City; reducing the commercial and residential routes with resulting annual savings; and the City Council hereby authorizes the execution and attestation by the City Manager and City Clerk.

SECTION 3. EXEMPTION FROM CEQA. The City Council finds, pursuant to Title 14 of the California Code of Regulations, Sections 15061(b)(3) and 15307, that this ordinance is exempt from the requirements of the California Environmental Quality Act (CEQA) in that it is not a project which has the potential for causing a significant effect on the environment and is a regulatory action as authorized by state law.

SECTION 4. CONSTITUTIONALITY; SEVERABILITY. If any section, subsection, sentence, clause or phrase of this ordinance is for any reason held to be invalid by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this ordinance. The City Council declares that it would have adopted this ordinance and each section, subsection, sentence, clause and phrase thereof irrespective of the fact that any one or more section, subsection, sentence, clause or phrase be declared invalid.

SECTION 5. EFFECTIVE DATE. This ordinance shall be in full force and effect thirty (30) days from and after the date of its adoption.

SECTION 6. POSTING AND PUBLICATION. The City Clerk is directed to cause copies of this ordinance to be posted in three (3) prominent places in the City of Sunnyvale and to cause publication once in *The Sun*, the official newspaper for publication of legal notices of the City of Sunnyvale, of a notice setting forth the date of adoption, the title of this ordinance, and a list of places where copies of this ordinance are posted, within fifteen (15) days after adoption of this ordinance.

Introduced at a regular meeting of the City Council held on _____, 2011, and adopted as an ordinance of the City of Sunnyvale at a regular meeting of the City Council held on _____, 2011, by the following vote:

AYES:

NOES:

ABSTAIN:

ABSENT:

ATTEST:

APPROVED:

City Clerk

Mayor

Date of Attestation: _____

(SEAL)

APPROVED AS TO FORM AND LEGALITY:

David E. Kahn, City Attorney

FIRST AMENDMENT TO
EXTENDED AND SECOND RESTATED AGREEMENT BETWEEN
CITY OF SUNNYVALE
AND
BAY COUNTIES WASTE SERVICES, INC.
FOR SOLID WASTE COLLECTION AND RECYCLING

This First Amendment (the "First Amendment") is dated as of September 30, 2010, and is an amendment to that certain Extended and Second Restated Agreement Between City of Sunnyvale and Bay Counties Waste Services, Inc. For Solid Waste Collection And Recycling, dated January 11, 2005 (the "Agreement").

The City of Sunnyvale and Bay Counties Waste Services, Inc. agree that the Agreement shall be amended as follows:

1. Section 3.03 of the Agreement is deleted and replaced by the following:

"3.03 Term of Franchise

The term of the franchise granted under this Agreement, as distinct from the Term of this Agreement, is 30 years, commencing at 12:01 a.m. on July 1, 1991 and expiring at midnight June 30, 2021.

If this Agreement is terminated earlier than its expiration, the Franchise will also terminate concurrently therewith."

2. Section 4.02 of the Agreement is deleted and replaced by the following:

"4.02 Term

The Term of this Agreement begins on December 1, 1990 and ends at midnight June 30, 2021."

3. Section D of Exhibit 8.03D is deleted and replaced by the following:

"D. Termination of Certain Incentive Payments. Contractor received Incentive Payments under the Incentive Program during the July 1, 1996-June 30, 1997 year that are payable with respect to cost savings programs implemented in prior years that resulted in savings in (i) Residential refuse collection labor (the "Residential Refuse Collection Incentive Payment") and (ii) workers' compensation insurance (the "Workers' Compensation Incentive Payment"). Notwithstanding any other provision of

this Exhibit 8.03D, but without prejudice to Contractor's right to receive other Incentive Payments (to the extent applicable under this Exhibit 8.03.D) beyond June 30, 2004, the Residential Collection Incentive Payment and the Workers' Compensation Incentive Payment terminated on June 30, 2004.

Contractor received Incentive Payments under the Incentive Program during the July 1, 2009-June 30, 2010 year that are payable with respect to an automation and route restructuring cost savings program implemented in a prior year that resulted and will in the future result in savings in Residential refuse collection costs (the "Residential Route Reduction Incentive Payment"). The Contractor Payment for the July 1, 2010-June 30, 2011 year anticipates a \$126,559.24 Residential Route Reduction Incentive Payment to Contractor. Notwithstanding any other provision of this Exhibit 8.03D, but without prejudice to Contractor's right to receive other Incentive Payments (to the extent applicable under this Exhibit 8.03.D) beyond June 30, 2010, the Residential Route Reduction Incentive Payment will be limited to a maximum of \$32,706 per year, effective July 1, 2010 and will terminate no later than June 30, 2021.

4. During the July 1, 2009-June 30, 2010 year, Contractor operated ten "commercial" front-loader garbage collection routes per weekday (Department 10). Contractor's equipment replacement schedule anticipates replacement of two of these front-loader garbage trucks during the July 1, 2010-June 30, 2011 year at a projected purchase price of \$402,196 per truck. Contractor agrees to purchase no more than one of these trucks and to reduce the number of Department 10 commercial front-loader garbage routes to no more than nine per weekday, effective September 1, 2010.

5. During the July 1, 2009-June 30, 2010 year, Contractor operated nine residential garbage collection routes per weekday (Department 30). Contractor's equipment replacement schedule anticipates replacement of nine of these residential garbage trucks during the July 1, 2011-June 30, 2012 year at a projected purchase price of \$378,816 per truck. Contractor agrees to reduce the number of Department 30 residential garbage routes to no more than eight per weekday, effective on the first day of the first calendar month, or the fifteenth (15th) day, whichever is sooner, after the Amendment to this Agreement inserting this provision is approved by City's City Council and signed by City, and to purchase no more than eight residential garbage collection trucks in the July 1, 2011-June 30, 2012 year."

6. Section 11.03 of the Agreement is deleted and replaced by the following:

"11.03 Possession/Purchase of Property Upon Termination

A. In Event of Default. If City terminates this Agreement in accordance with Section 11.02, City may take possession of any and all of Contractor's Service Assets and use those Service Assets to collect and transport any Solid Waste generated within City. City may retain the possession of those Service Assets until other suitable arrangements can be made for the provision of Solid Waste collection services, including the grant of a franchise to another solid waste hauling company.

B. Upon Expiration of this Agreement. At midnight on June 30, 2021 (the "Expiration Date"), Contractor shall transfer to City title, ownership or other rights to use and possession (such as leasehold interests in the case of leased Service Assets) and possession of all, but not part, of the Service Assets (excluding land, buildings and fixtures), without encumbrance or lien other than those in existence as of the date Contractor executed the Agreement and liens for property taxes not yet due and payable. Waste Generators' possession of Containers will be deemed possession by City for this purpose. CITY'S PURCHASE OBLIGATION WILL SURVIVE THE EXPIRATION OF THIS AGREEMENT.

1. Service Assets To Be Purchased

Service Assets subject to the City's obligation to purchase are those listed by department below and refer to those assets shown in the Equipment Depreciation Schedules that are part of the approved Contractor Payment Request for Fiscal Year 2009/10 and future modifications to those schedules approved by City.

- Department 10 (Commercial FEL) - All items
- Department 20 (Commercial Roll-Offs) - All items
- Department 30 (Residential Collection) - All items
- Department 40 (Commercial/Industrial Recycling) - All items
- Department 50 (Yard Waste Recycling) - All items
- Department 70 (Multi-Family/Residential Recycling) - All items
- Department 80 (Vehicle Maintenance) - No items
- Department 90 (Container Maintenance) - Container and lift trucks only

- Department 00 (Administration) - Pickup trucks and phone system only
2. Adjustments to asset purchase schedules

Contractor and City shall work cooperatively to adjust asset purchases between the date of this First Amendment and the Expiration Date in order to minimize the purchase price of the Service Assets required to be purchased by the City on the Expiration Date; provided, however, that Contractor shall be compensated by means of increased Contractor's Payments for the increased cost, if any, of maintaining Service Assets that are not replaced on schedule and continue to be used after their scheduled replacement dates. Any assets scheduled to be replaced within 2 years of the Expiration Date shall not be replaced without the prior written approval of City.

3. Contractor Obligation To Maintain Assets

Contractor agrees to maintain, use and repair all Service Assets that are subject to the City's obligation to purchase in accordance with the manufacturers' specifications. Contractor agrees to provide City with maintenance records for such Service Assets to be purchased prior to City purchase. City shall have the option, at City expense, to perform an inspection of such Service Assets prior to purchase. Service assets that have not been maintained in accordance with the manufacturers' specifications or that are non-functioning shall not be subject to City's purchase obligation.

Simultaneously upon City's purchase of the Service Assets subject to City's obligation to purchase, City shall pay Contractor an amount equal to the aggregate depreciated value of such Service Assets (as used for determining the Contractor Payment amount subject to City approval per the Agreement) at Agreement expiration. Any of such Service Assets the purchase price for which has been fully paid to Contractor through Contractor's Payments shall be transferred at no cost to City.

C. Records and Service Asset Documentation. Upon City direction, Contractor will furnish City with immediate access to Waste Generator subscription (including service and complaint information), routing, and all of its business records related to its billing of accounts for services that are not billed by City under Section 6.01A. Contractor will comply with its obligations with respect to Service Asset Documentation as defined in and in accordance with Section 10.01B.

D. Undepreciated Assets. Except as set forth in part B of this Paragraph 11.03, Contractor has no right to

recover amounts equal to any undepreciated asset value remaining upon expiration or earlier termination of this Agreement from City or Waste Generators."

7. Exhibit 8.03A Section [C2]a. Escalation of Fuel is amended by replacing the incorrect reference to "05-73-02-01 Producer Price Index #2 Diesel Fuel," with the correct reference "05-73-03 Producer Price Index #2 Diesel Fuel."

8. Section 1.03N2 of Exhibit 5.02 is deleted and replaced by the following:

"Disabled and Elderly Rear Yard Service; Push Out Service.

Contractor may enter onto private property to provide rear yard services to the disabled or elderly in accordance with Section 1.04B and push out service to Waste Generators who subscribe to push out service in accordance with Section 1.030."

9. Section 1.06A1 of Exhibit 5.02 is deleted and replaced by the following:

"1.06. Commercial/Industrial Collection - Can Service, Bin Service and Drop Boxes/Compactors

A. Service Provided.

1. Frequency and Commencement.

Contractor will collect all Solid Waste at Commercial/Industrial premises at least once each week, Monday through Saturday, commencing on the next regularly scheduled collection day following that Commercial/Industrial Waste Generator's request for service. Contractor will provide push out service described in Section 1.030 of this Exhibit at request of Commercial/Industrial Generators at rates established by City.

Contractor will provide special collection services as requested by the Commercial/Industrial Waste Generator at rates established by City."

10. Section 8.03A2 of the Agreement is amended by changing contract year references as follows:

Reference(s) to (PAC06) are changed to (PAC14)

Reference(s) to (P6) are changed to (P14)

Reference(s) to (PL6) are changed to (PL14)

Reference(s) to (PV6) are changed to (PV14)

Reference(s) to (PO6) are changed to (PO14)
Reference(s) to (NID6) are changed to (NID14)

11. Except as amended by this First Amendment, the Agreement shall remain in full force and effect in accordance with its terms.

IN WITNESS WHEREOF, City and Contractor have executed this First Amendment as of the day and year first above written.

ATTEST:

CITY CLERK

CITY OF SUNNYVALE ("City")

By:

Kathleen Franco-Simmons
City Clerk


Melinda Hamilton
Mayor

APPROVED AS TO FORM:

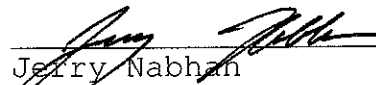
David Kahn
City Attorney

BAY COUNTIES WASTE SERVICES,
INC. ("Contractor")

By:


Robert Molinaro
President

ATTEST name and signature:


Jerry Nabhan
Corporate Secretary