

April 21, 2023

Metro
600 NE Grand Avenue
Portland, OR 97232-2736

Subject: Review of Fiscal Year 2023-2024 Solid Waste Disposal Fees

Dear Ms. Madrigal, Chief Operating Officer,

Metro engaged FCS GROUP to provide an independent review of the methodology for calculating proposed solid waste disposal fees for Fiscal Year (FY) 2023-2024. In response to this request, we have reviewed Metro's updated Excel Fee Model (Model) and associated fees for accuracy, adequacy, reasonableness and compliance with industry practices. This review is in accordance with *Metro Code – Title V Solid Waste Section 5.03.070 "Independent Review of Fee Setting Process; Written Report"*.

This review focused on the overall methodology and resulting fees for compliance with industry practices for FY 2023-2024. The review did not validate the accuracy of source documents or formulae and structure utilized in the Model.

The FY 2023-2024 findings and comments are summarizing below:

- The methodology utilized in the fee setting process follows best practices in the industry. The overall analysis is structured around three (3) fee setting components, or steps:
 1. *Revenue requirement*: evaluates the overall revenue needs of the utility on a self-supporting basis, considering operating and maintenance expenditures, capital/equipment funding needs, debt requirements and fiscal policies.
 2. *Cost of service*: equitably distributes costs to services based on their proportional demand and use of the system.
 3. *Rate / fee design*: includes the development of fees that generate sufficient revenue to support the revenue requirement and address Metro's policy goals and objectives.
- The recommended overall fee strategy (step 1, revenue requirement) for FY 2023-2024 projects revenues after increase to be below annual operating obligations, requiring the use of \$600,000 in reserves. When evaluating reserve levels, it is important to recognize that the value of reserves lies in their potential use. A reserve strategy that deliberately avoids any use of reserves negates their purpose. Fluctuation of reserve levels may indicate that the system is working, while lack of variation over many years may suggest that the reserves are, in fact, unnecessary. The benefit of projecting revenue requirements beyond the immediate test year period is the ability to level out impacts over time, if necessary. The Model does project the revenues after increase for subsequent years to meet the estimated revenue needs, assuming the proposed fees are implemented.
 - » The operating and maintenance (O&M) expense projection for this year's Model update does include a budget realization factor of approximately 95 percent. The budget realization factor reduces the overall budget, not including cost allocation plan expenditures, down to 95.0

percent of the total. This practice is common in the rate setting industry and is often utilized if a utility has historically expended less than planned or if the utility anticipates the test year to be below budget due to factors identified after the budget has been adopted. The budget realization factor reduces the overall operating budget by approximately \$6.0 million for the FY 2023-2024 test year. Metro should continue to closely monitor actual annual expenditures compared to the figures used in the current rate strategy and adjust if necessary.

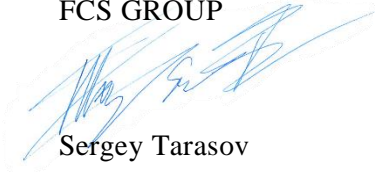
- The cost allocation (step 2, cost of service) utilized in developing service level charges appears technically sound and consistent with that deemed acceptable by industry practices. Costs appear to be allocated with cost causation principles, mimicking the nature of how they are incurred. Primary allocation occurs based on actual time spent by employees within each service level, contractual costs associated with each service level or a direct assignment of costs to a specific service level.
 - » For this year's update, Metro has expanded the O&M expense line-item budget used in the Model. The greater detail allows Metro to hone in on individual expenses, which may have been grouped within larger summary level categories. The expanded approach may increase the granularity of cost allocation but may require additional time for tracking and future updates. Overall, this adjustment did not have a material impact on the cost allocation results.
 - » Another change that has occurred with this year's update is the allocation of the Operating and Personnel cost components of the Central and South Transfer Station contracts. In prior studies, these cost elements were allocated based on the working floor area for each transfer station and the associated service. The updated allocation distributes these costs based on FTEs assigned to each service within the transfer station. While this is a change from prior studies, this modification has been made to more closely align with the actual expenses incurred. The results of this change shifts cost recovery towards scalehouse operations and impacts the cost-based transaction fee.
 - » The results of the cost-of-service analysis indicate that cost differences are present between existing fees and the cost-based allocation. It should be noted that, typically, if the result of each individual service is within plus (+) or minus (–) 5.0 to 10.0 percent of the overall system average, they are generally considered to be within cost-of-service. This range of reasonableness is given since although there is an industry accepted methodology, the specific classification and allocation of expenses reflect cost and waste characteristics at a given point in time. With time, waste patterns, composition and facility requirements change resulting in changes to cost-of-service. The flexibility to work within the range of reasonableness can minimize annual peaks and valleys and help maintain stable fees from year to year.
- The proposed fees (step 3, rate / fee design) phase-in cost-of-service results over a 5-year period. Staffed and automated fees, mixed solid waste, clean wood and residential organics are phased-in to within 4.0 percent of their cost-of-service level, with the majority projected to be within 1.0 percent. By the end of the 5-year period, commercial organics are projected to be within 7.0 percent of their cost of service, which falls in line with the 10.0 percent range of reasonableness discussed above. The yard waste fee is held below allocated costs, to support programmatic goals for this waste area.
 - » The proposed rate design, when reconciled with projected billing units, does project a lower revenue generation in comparison to the total revenue requirement targets identified in step 1, revenue requirement. The deficiency ranges from \$2.0 million in FY 2023-2024 down to

\$113,000 in FY 2027-2028. While the rate design does generate less revenues, effectively lowering the overall rate increases identified in step 1, Metro's existing fund balances are projected to be sufficient to cover the deficiency.

We appreciate the opportunity to work with Metro on this project. Please do not hesitate to contact me if you have any questions regarding this letter or if additional information is needed.

Sincerely,

FCS GROUP



Sergey Tarasov

Principal

cc: Financial Planning Director Cinnamon Williams, Chief Financial Officer Brian Kennedy, and Councilors Peterson, Simpson, Lewis, Rosenthal, Gonzalez, Nolan and Hwang