



DATE: July 15, 2013

TO: Honorable Mayor and City Councilmembers

FROM: Patrick Klaers, City Administrator

SUBJECT: Franchise Fees

Introduction

When the City Council discussed the Capital Improvement Program (CIP) in the summer of 2012, concerns were again raised about not having sufficient funds to do all the projects that were included within the 5 year plan and to do all the projects that are needed in the long term. Later in the year, the Council approved a “fiscally constrained street CIP” and discussed the benefits and drawbacks associated with a franchise fee program. At that time, in October 2012, staff was directed to follow up on the possibility of establishing a utilities franchise fee.

Background

Earlier this year I discussed franchise fees with neighboring City Managers/Administrators and learned that Mounds View and New Brighton have existing franchise fee programs and that Shoreview was considering a franchise fee program (since approved in May, 2013). Sue Iverson, Director of Finance and Administrative Services, has worked with the Ramsey County staff and did some preliminary research on our City tax base composition. This past spring, I contacted Colette Jurek, Manager – Community & Local Government Relations, for Xcel Energy to discuss the City’s interest in evaluating a franchise fee program and on May 1st Colette sent me some preliminary data on gas and electric revenues based on a 1% amount that was converted into a flat fee plan.

The City Council discussed the possibility of establishing a franchise fee program during the June 17, 2013, work session. The need for additional revenues to address the City’s CIP goals and to address the City’s street and trail infrastructure maintenance issues was discussed. Benefits of a franchise fee program were reviewed and included:

- Establishes a new revenue source which diversifies the City’s revenue base.
- Will generate a significant amount of revenue that could not be raised from property taxes alone.
- May reduce the growing pressure on taxpayers in the community for more revenues.
- The new revenues provide an opportunity to address the City’s infrastructure needs.

Attached for your review is the May 1st material from Colette Jurek and the follow up material from Colette dated June 14, 2013. This June 14th material includes customer counts by classification and also provides information on how to locate on the Xcel website the list of communities within the Xcel service territory where franchise fees are currently being collected.

Discussion

According to Colette, Xcel prefers that communities identify a percentage that it wants to collect or a dollar amount that is needed from franchise fees, and then this percentage or amount is converted into a flat fee monthly rate. A flat fee rate is preferred to a percentage fee in order to even out the “highs and lows” in the monthly bills due to weather conditions and make the monthly fee a predictable amount for the customers. Each customer in a classification would pay the same amount regardless of usage or property value. According to the Xcel list of communities where franchise fees are collected, this flat fee approach is by far the most common approach used.

Based on the figures included in the May 1st material and conversations with Colette on appropriate guidelines for franchise fee revenues, combined with the feedback from the Council during the June 17th work session, the Director of Finance and Administrative Services developed the following chart:

	Estim # of Accts	1.00% Rate	Franchise Revenue	2.75% Rates	Franchise Revenue	% of Revenue Generated by Class
Electric						
Residential	3051	\$ 1.00	\$ 36,612	\$ 2.75	\$ 100,683	22.79%
Commercial/Industrial, small non-demand	190	\$ 1.25	2,850	\$ 3.44	7,838	1.77%
Commercial/Industrial, small demand	173	\$ 15.25	31,659	\$ 41.94	87,062	19.71%
Commercial/Industrial, Large	60	\$ 123.75	89,100	\$ 340.31	245,025	55.47%
Street lighting	17	\$ 1.25	255	\$ 3.44	701	0.16%
Municipal pumping non-demand	2	\$ 4.00	96	\$ 11.00	264	0.06%
Municipal pumping demand	10	\$ 0.50	60	\$ 1.38	165	0.04%
Total	3503		\$ 160,632		\$ 441,738	100.00%
Gas						
Residential	2720	\$ 1.00	\$ 32,640	\$ 2.75	\$ 89,760	55.64%
Commercial firm non-demand	285	\$ 5.00	17,100	\$ 13.75	47,025	29.15%
Commercial firm demand	1	\$ 18.00	216	\$ 49.50	594	0.37%
Small interruptible	6	\$ 61.00	4,392	\$ 167.75	12,078	7.49%
Medium & large interruptible	3	\$ 120.00	4,320	\$ 330.00	11,880	7.36%
Transportation firm	0	\$ 120.00	-	\$ 330.00	-	0.00%
Transportation interruptible	0	\$ 120.00	-	\$ 330.00	-	0.00%
Total	3015		\$ 58,668		\$ 161,337	100.00%
Estimated Franchise Revenue			\$ 219,300		\$ 603,075	

The data in this chart shows that the electric customer would pay 73.25% and the gas customers would pay 26.75% of the total amount of franchise fees collected. Each residential customer would pay \$2.75 per month for electric and \$2.75 per month for gas. The electric residential customer pays 22.79% of the total electric franchise fee and the gas residential customer pays 55.64% of the total gas franchise fee. Combined, the residential customer pays 31.58% of the total franchise fee collected. (This will show up as a **City Fee** on all the customer bills.)

Based on a franchise fee of 2.75 percent converted to a flat fee plan, the City is expected to receive \$603, 075 in new revenue. To compare the impact to the home owner for the annual franchise fee (\$2.75 x 2 = \$5.50 x 12 = \$66 per year) verses an increase in the property taxes to generate this same \$603,075 amount, the Director of Finance and Administrative Services has developed the following chart:

\$603,075 Annual Revenue Generated from Franchise Fee versus Property Tax				
Home Market Value	Home Value After MVE	Cost per Home Franchise Fee	Property Tax	Cost Difference
\$ 140,550	\$ 115,959	\$ 66.00	\$ 66.00	\$ -
\$ 200,000	\$ 243,326	\$ 66.00	\$ 102.89	\$ 36.89
\$ 257,400	\$ 243,326	\$ 66.00	\$ 138.46	\$ 72.46
\$ 350,000	\$ 344,260	\$ 66.00	\$ 195.94	\$ 129.94
\$ 500,000	\$ 500,000	\$ 66.00	\$ 284.55	\$ 218.55
\$ 750,000	\$ 750,000	\$ 66.00	\$ 462.40	\$ 396.40
\$ 900,000	\$ 900,000	\$ 66.00	\$ 569.10	\$ 503.10

As you can see in the above chart, the impact to home owners for generating revenues of \$603,075 to home owners is typically less with a franchise fee verse increasing the City tax rate.

It should be noted that when the franchise fee is converted to a flat fee rate, then the rate does not change over time. There is no inflation factor added annually. The only growth in the total fee collected for the City would come from new development; such as what is planned to happen on TCAAP.

*Uses of the Funds...*The staff memo for the June 17th work session included comments on the need to move the street maintenance and trail rehabilitation expenses out of the PIR fund as these are really operating expenses and not capital expenses. Moving this expense out of the PIR Fund increases the chances that the General Fund transfer to the PIR Fund will be spent on the PMP program. Since the General Fund cannot absorb these expenses without impacting other City services, this funding of street and trail maintenance expenses with franchise fee revenues is a top staff priority. Additionally, the equipment capital fund needs financial help and it is

reasonable to have the franchise fee help pay for some of the equipment that does the street and trail maintenance work.

The use of the franchise fees can change at any time depending on Council action, but the idea discussed on June 17th was to establish a separate fund for the franchise fees and only use the fund for specific activities – most of which would be capital in nature and/or infrastructure related. While the use of the fund can be decided later, below is a list for the Council to consider:

- Street Maintenance (seal coat and crack filling) \$150,000 per year
- Trail Rehabilitation \$ 50,000 per year
- Equipment Fund Contribution \$ 40,000 per year
- Park Equipment Replacement \$ 60,000 per year
- City Hall Reserve – Maintenance/Improvements \$100,000 per year
- Reserve for future CIP expenses \$203,075 per year

It seems appropriate that the “reserve for future CIP expenses” money go toward our pedestrian pathway system to help make the entire community accessible for walkers and bikers and to connect our City to the regional systems that are near our boundaries. It should be noted that a trail between Highways 96 and 51 along old Highway 10/Snelling could cost in excess of \$2 million and a trail connection from the CR E bridge to the beach could be in excess of \$1.5 million (and to extend the trail/pathway to the eastern or southern City limits would be another \$500,000 each). Pathways are important but they are also expensive!

Additionally, on June 17th there were some comments made regarding dedicating some of the franchise fee revenues toward public safety expenses.

Approval Process... In order to approve a franchise fee program, the City Council will need to amend the existing Electric Franchise ordinance and the existing Gas Franchise ordinance. Both of these ordinances were approved on November 30, 2009, and they granted the company rights for a period of 20 years. No public hearing is required to amend these ordinances. After adoption of the ordinances, Xcel will need at least 90 days to implement the franchise fee. Xcel will collect the franchise fee revenues and make quarterly payment to the City.

Public Involvement... While no public hearing is required for adoption of the franchise fee ordinance amendment, the Council may want to consider accepting public comments on the proposal as there are bound to be people for the program (especially if some funds are dedicated to pedestrian pathways) and some people against the program.

Questions...

- Does the Council want to move forward with the franchise fee program? If so, at what amount?
- Does the Council like the flat fee method that is recommended by Xcel?
- How does the Council want to take public comments on the proposal?
- The electric classes of Small C&I Non-Demand and Small C&I Demand and the gas class of Commercial Firm: Non-Demand are big contributors into the franchise fee fund;

so what types of customers are in these classes? What information can Xcel provide us on these customers?

- Does the Council support financing street and trail maintenance and some equipment with the new revenues?
- Does the Council want to decide how to use the new revenues now or consider the issue at a future meeting?

Colette Jurek will be at the July 15th Council work session to provide information on franchise fees, to answer questions that the Council has regarding a franchise fee program, and to review the process for establishing a franchise fee program.

Attachments

Attachment A: Correspondence from Colette Jurek dated May 1, 2013.

Attachment B: Correspondence from Colette Jurek dated June 14, 2013.