




Memorandum

MONTEREY REGIONAL WASTE MANAGEMENT DISTRICT

Reviewed by: 
General Manager

Date: 9/11/2020

DATE: September 11, 2020
 TO: General Manager
 FROM: Director of Engineering & Compliance
 SUBJECT: Authorize \$2.5 million in Site Improvements for compost area operations and approve 10-year contract and lease extension with Gabilan AG Services.

RECOMMENDATION: a) Authorize Site Improvements of Compost Area Operations in the Amount of \$2.5 million dollars and; b) Approve 10 Year contract and Lease Extension with Gabilan AG Services.

BACKGROUND

In August 2015 the California Regional Water Quality Control Board (RWQCB) issued the final waste discharge requirements for standardization of minimum standards of design and operations of compost facilities in California. Heretofore, compost facilities were permitted individually by the separate RWQCB Regions. The 2015 General Order Waste Discharge Requirements (WDR) for Composting Operations (Order WQ 2015-0121-DWQ) defined the design and operations minimum standards and a five (5) year implementation period for existing permitted compost facilities like the Gabilan AG Service's facility at the District. As the permit holder since 2009, on a year-to-year lease term basis, Gabilan AG Services (aka Keith Day Company, Inc.) has been/is responsible for the design and operations of the compost facility. Over the past two (2) years they have been coordinating with consultants and the RWQCB to develop the design, operations plans, and schedule necessary for compliance with Order WQ 2015-0121-DWQ. Not only for the District's site but also for two (2) other sites in southern Monterey County. The RWQCB is requiring that implementation of the General Order WDR requirements be completed in FY20/21.



DISCUSSION

The scope of this report is twofold: namely a) authorize \$2.5 million of capital funds for regulatory required physical site improvements of the District's compost area, and b) approval of Staff's development of a ten (10) year lease with the compost facility's operator/permit holder, Gabilan AG Services. These two elements will be presented separately below.

Site Improvements

In anticipation of the compost area site improvements needed to comply with the RWQCB General Order WDR, Staff had budgeted approximately \$5 million in the FY18/19 budget when the scope of the improvements was not known to any great detail and \$2 million in FY19/20 when there was some conceptual level design information known. These budgeted funds were not spent as the design and permitting of the improvements had not yet been developed by Gabilan AG Services with the RWQCB. Those design and permitting details for the site improvements have now been proposed and are presently under review by the RWQCB at this time. The major site improvements consist of a large pond with a liner system to capture the storm water runoff from the entire site area, surface grading to obtain a stable, relatively low permeability working surface for the compost operations, and electrical and water utility services. These improvements are estimated to cost \$2.5 million.

Staff recommends that the Board authorize a capital expenditure of \$2.5 million for the compost area site improvements to accomplish the regulatory requirements of Order WQ 2015-0121-DWQ. Staff proposes that the \$2.5 million capital expenditure will be accomplished without a net change to the FY20/21 approved budget. This would be accomplished by i) deferring \$2.5 million in spending for the Module 7 project, and ii) reallocating that approved funding to the regulatory required compost area site improvements.

Compost Operations

Since 2009, Gabilan AG Services has been operating the District's composting facility. They took over the operation when the Venture Capital group that had bought out the prior permit holder went bankrupt and abandoned the operations of the compost facility. Since that time the District and Gabilan AG Services have operated on a year-to-year lease term and have periodically negotiated the processing rate charged to operate the compost facility for inflationary costs and any costs associated with a change in the scope of the services. Over that time, Gabilan AG Services has almost seamlessly expanded its services of yard waste, clean wood waste, and most recently, following the planned termination of the AD Pilot Project in 2019, food waste upon the request of, and for the benefit of, the District and its member communities. Gabilan AG Services has made strategic hires of both an operations manager and CFO. They have three (3) facilities in Monterey County including the District's site. In the past year or so, Gabilan has invested about \$3 million in capital equipment for the District's site. In addition, the District has spent or committed to spend almost \$100k for design and permitting costs associated with the RWQCB General Order WDR requirements for design improvements to the District's compost facility.

For these reasons, and the proposed \$2.5 million capital improvement expenditure proposed by the District for the site improvements, Staff recommends that a minimum ten (10) year lease agreement be developed for the individual and mutual interests of both the District and Gabilan AG Services. The ten (10) year lease term would be commensurate with capital expense recovery for both parties and would provide both parties certainty of operations over that period of time. As has been the case for the past eleven (11) years, the processing rate charged to the District would be a mutually negotiated rate that is primarily based on inflationary costs and any capital expense recovery for changes in service scope. The historical processing rates have proven to be fair and reasonable and competitive in that market. Staff recommends developing the longer-term lease term to provide some certainty for the operations during this decade as SB1383 implementation is undertaken. Staff recommends that the Board authorize staff to negotiate a 10-year contract and lease extension to Gabilan AG Services as outlined in the table below. Based on the Board's approval of the general terms cited below, Staff would develop a specific contract and lease document in a form satisfactory to the General Manager and Legal Counsel prior to bringing to the Board for final approval.

ITEM	EXISTING LEASE CONDITION	PROPOSED LEASE CONDITION
Initial Lease Term	1 Year	10 Years
Lease Extension Term	1 Year; not limited	5 Years; limited to two (2) extensions
Rate Change - Inflation Costs	Periodic; Mutually negotiated amount	Annually; Mutually negotiated rate
Rate Change – Service Scope Change	As Occurs; Mutually negotiated amount	As Occurs; Mutually negotiated amount
Land Lease Amount	Monthly; \$3,733.42	Monthly; to be mutually determined
Lease Area	Variable: Area has decreased in size	Fixed; Define current area

FINANCIAL IMPACT

Funds for the compost facility site improvements were purposely not included in the FY 20/21 capital improvement budget until the scope of the site improvements became known with greater certainty. Gabilan AG Services has recently submitted design plans to the RWQCB for their review and approval. Construction of these site improvements on District property are estimated to cost \$2.5 million. Given that waste filling of Module 6 is just now starting, the construction of Module 7 can be deferred at this time and the budgeted funds reallocated to the compost facility project. Thus, there would be no net change to the FY20/21 capital improvement budget that has been approved by the Board for FY20/21.

The current Lease Processing Rate of \$25/ton charged to the District by Gabilan AG Services and the District’s Tip Fees of \$42/ton for Clean Yard and Wood Wastes and \$57/ton for Food Wastes charged to customers in FY20/21 would not change. No impact. If Gabilan AG Services was the party investing \$2.5 million into the improvements to the District’s compost area, an approximate \$4/ton increase to the current \$25/ton processing rate charged to the District would be expected to occur. However, Gabilan AG Services is not in the position to make this expenditure and it is in the District’s interest to accomplish the site improvements to satisfy the regulatory requirements and keep the composting process operating.

To determine if the \$2.5 million capital expenditure is a beneficial investment, Staff evaluated several perspectives to provide a context to the Board of the value to the District of the Gabilan AG Services compost operations. Staff evaluated i) compost processing rates at other sites, ii) estimated costs of a District operated facility onsite, and iii) costs to the District of sending the waste materials offsite to a 3rd Party compost operator.

Compost processing rates at other sites were found to be in the \$25 - \$30/ton range and higher. The current rate of \$25/ton is on the low end of that range and is deemed competitive.

Staff evaluated the alternate scenario of using District staff and equipment to perform composting onsite instead of having a lease with Gabilan AG Services. This analysis showed that the District’s labor costs alone would be equivalent to the total processing fees charged to the District by Gabilan. Adding capital equipment and maintenance expenses to this option result in a significantly more costly alternative for the District.

The alternative of sending all the materials offsite to a 3rd party compost operator was found to be in the \$65 - \$90/ton cost range. This alternative also assumed that there would exist a 3rd party operator that had sufficient permit capacity authority to be able to receive all of the District’s materials. Thus, this alternative was not deemed to be a financially beneficial alternative.

CONCLUSION

The District has had eleven (11) years of mutually beneficial experience with Gabilan AG Service's operations of the compost facility. During this period, Gabilan AG Services has incorporated expanded services of wood grinding and processing, yard waste processing, and most recently, food waste processing for the District and to the benefit of the District. This has occurred with a year-to-year lease and negotiated pricing of competitive rates during that time. Now that Gabilan AG Services has invested approximately \$3 million in operations equipment and permitting, and the District proposes to invest \$2.5 million in site improvements, the parties have both individual and mutual interests to commit to a minimum ten (10) year lease agreement commensurate with these investments. Therefore, Staff recommends that the Board authorize FY20/21 funding for regulatory required site improvements of the onsite compost facility in the amount of \$2.5 million and approval of general lease conditions for Staff's subsequent development of a 10-year lease agreement with the compost facility operator and permit holder, Gabilan AG Services (aka Keith Day Company, Inc.), for continued operations of the onsite compost facility.


Guy R. Petrabor