



Christine O. Gregoire

ATTORNEY GENERAL OF WASHINGTON

Utilities and Transportation Division

1400 S Evergreen Park Drive SW • PO Box 40128 • Olympia WA 98504-0128 • (206) 753-2281

August 15, 1994

Steve McLellan, Secretary
Washington Utilities and
Transportation Commission
1300 S. Evergreen Park Drive S.W.
P.O. Box 47250
Olympia, Washington 98504-7250

Re: King County v. Seattle Disposal
Docket No. TG-940411

Dear Mr. McLellan:

Enclosed please find the original and nineteen copies of the Brief of the Commission Staff in the above-reference matter. Please accept the same for filing.

Very truly yours,

ANNE E. EGELER
Assistant Attorney General

Enclosure

cc: All parties

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UTILITY AND TRANSPORTATION
COMMISSION



BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

KING COUNTY DEPARTMENT OF PUBLIC WORKS, SOLID WASTE DIVISION, Complainant, vs. SEATTLE DISPOSAL COMPANY, RABANCO LTD., d/b/a EASTSIDE DISPOSAL AND CONTAINER HAULING, Respondent.

DOCKET NO. TG-940411

BRIEF OF COMMISSION STAFF

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I. STATEMENT OF THE FACTS

On December 28, 1993, Seattle Disposal Company, d/b/a Eastside Disposal and Container Hauling (Eastside) filed a request with the Washington Utilities and Transportation Commission (Commission) to increase its rates for residential and commercial solid waste, and residential curbside recycling collection service. (Docket No. TG-931585). Eastside sought increased rates to enable the Company to recover increases in wages, recycling costs, and business and occupation taxes.

The Commission Staff (Staff) audited Eastside's books and records, using a test year ending June 30, 1993. After investigating the underlying financial information, the Staff made numerous pro forma and restating adjustments to reflect known changes in the Company's revenue and expenses. Ex. 96-2, p. 3-6. Based on its calculations, the Staff recommended that the Commission approve a rate increase, but at a level lower than the

request filed by the Company. Id. at 2. The rates recommended by the Staff were based on the cost of providing service at each service level. Prior to 1994, Eastside's rates were not based on the cost of providing service.

On February 7, 1994, the Commission considered the proposed rate increase during an open public meeting. The rate increase was opposed by King County. The Commission accepted the rate recommendation made by the Staff, and increased Eastside's rates, based on the cost of providing service.

On March 23, 1994, King County filed a complaint against Eastside's rates. Four days of hearings were held before the Commission to consider the testimony and evidence presented by witnesses for King County, the Commission Staff, Eastside and members of the public.

II. ARGUMENT

There are two goals which the Commission is statutorily required to balance in this case. The Commission must consider the waste reduction and recycling goals of the Waste Not Washington Act. Second, the Commission must fulfill its obligation to regulate rates in the public interest. Although the need to encourage recycling is important, it would be a grievous error to view it as a moral imperative that eliminates the need to ensure that the public is protected from unfair or inflated rates.

The Commission accomplished both goals in setting Eastside's present rates, and established a rate structure which sends honest

price signals to the public, while encouraging participation in curbside recycling.

A. Eastside's Inclining Rate Structure Provides a Strong, Rational Incentive to Reduce and Recycle Waste.

In 1989, the Legislature passed the "Waste Not Washington Act", in an effort to reduce waste and promote recycling. Laws of 1989, ch. 431. The Act sets forth the general waste reduction goals of the state, and prioritizes the waste management options. RCW 70.95.010(8). Each county is directed by the Act to prepare a solid waste management plan addressing the manner in which the county will work to achieve the state's waste reduction and recycling goals. RCW 70.95.080. Although counties are given specific authority to control solid waste disposal facilities, they may only establish collection rates if they choose to enter a contract for residential collection of source separated recyclable materials.¹ RCW 81.77.230; RCW 36.58.040. If a county opts not to enter a collection contract, the authority to regulate solid waste carriers is vested solely in the Commission. The Waste Not Washington Act does not state how the Commission is to set rates.

¹ It should be noted that recent federal legislation calls into question the County's ability to control recycling rates. On August 8, 1994, both houses of Congress passed a bill deregulating intrastate transportation of property. If the bill is signed, 49 U.S.C. § 11501 will be amended to pronounce that states, and political subdivisions of states, are preempted from regulating intrastate transportation of property. At this time, it is uncertain what impact this will have on the authority of the state and counties to regulate collection of recyclable material.

1. The Commission has approved rates which are consistent with the solid waste priorities provided in RCW 70.95.010.

RCW 70.95.010(8) is the portion of the Waste Not Washington Act which prioritizes solid waste collection, management, and handling options in the following descending order:

- (a) Waste reduction;
- (b) Recycling, with source separation of recyclable materials as the preferred method;
- (c) Energy recovery, incineration, or landfill of separated waste;
- (d) Energy recovery, incineration, or landfilling of mixed wastes.

RCW 81.77.030(6) states that the Commission must set rates that are consistent with the general solid waste management priorities set forth in RCW 70.95.010. At no point in the Act does the Legislature state that the Commission must use any means necessary to achieve the maximum possible waste reduction. The Act certainly does not instruct the Commission to abandon cost-based rates, and impliment misleading and dishonest price signals in an effort to coerce the public to recycle.

This Commission has worked hard to set rational, cost-based rates that comply with the spirit and the letter of RCW 70.95.010. The cost-based, variable rate structure that the Commission has approved for Eastside fully meets the requirements of RCW 70.95.010(8) by providing the public with a strong financial incentive to reduce waste and recycle. The rate for solid waste collection increases significantly at each service level. The

rates approved by the Commission contain a twenty-four percent increase between the mini and one-can rates, a twenty-nine percent increase between the one and two-can rates, and a thirty-eight percent increase between the two and three-can rates.² This rate structure furthers the state's goal of waste reduction by ensuring that customers that reduce their waste receive a substantial financial benefit.

Eastside's rate of customer participation in both the single and multi-family recyclables collection programs exceeds the goals set by King County. Ex. T-1, p. 21. Single-family customers have an impressive eighty-four percent participation rate. Multi-family customers have a sixty-one percent participation rate. Id. King County has not offered any evidence to suggest that the participation rates have been impacted in the six months following Eastside's rate increase. If the testimony provided by Eastside customers at the public hearing is any indication, participation rates will not decline. Although the customers complained about the rate increase, not a single one of them indicated that they intended to stop recycling and subscribe to a more expensive service level.

² The current percent differential between the service levels is incorrectly stated in the testimony of King County witness Hanson. Ex. T-RGH, p. 24-25. Mr. Hanson claims that he is stating the "percentage differentials between garbage collection service levels". Id. at 23. In reality, he is stating the percentage differentials between the combined rate for solid waste and curbside recycling, and comparing this to King County's proposed solid waste rate differentials.

In addition to charging an inclining rate for solid waste collection, Eastside has a mandatory, flat rate for curbside recycling. Since customers must pay for curbside recycling, they have an incentive to use the service. Customers that divert material into their curbside collection bins are able to reduce the level of solid waste service they subscribe to and decrease their solid waste bill. Since the recycling rate is flat, customers are able to increase their use of the curbside collection program without incurring an increased charge. This rate structure furthers the state's goal of increasing recycling. RCW 70.95.010(8)(b).

Waste reduction and recycling in Eastside's territory are further encouraged by the availability of a yard waste collection program. The yard waste collection program meets the goals of RCW 70.95.010(8) by providing residents with a convenient means to divert their yard waste from the solid waste stream. King County has argued that it is more expensive to subscribe to yard waste service than it is to dispose of yard waste, and therefore, people have a disincentive to recycle. In reality, King County has enacted local Ordinance 10942 banning yard waste from the waste stream. As a matter of law, customers must either subscribe to the yard waste program or compost their waste. King County did not offer any evidence to suggest that Eastside's customers are ignoring the law. Finally, as with recycling, yard waste is a flat rate service. Customers can set out as much yard waste as they

generate, without experiencing an increase in their bills.

King County has a yard waste participation goal of sixty percent. Id. Not surprisingly, customer participation levels have not met this goal. Forty to forty-five percent of the residents are composting some or all of their yard waste. Tr. 227. Some residents do not have a yard. Others pay for a lawn care service that disposes of their yard waste. Ex. T-88, p. 22. King County's participation goal is unrealistic, and inconsistent with the priorities set forth in RCW 70.95.010(8). The County should continue to place its emphasis on encouraging increased back yard composting, which decreases the generation of yard waste, rather than emphasizing waste collection.

Despite Eastside's inclining, variable rate structure, the mandatory recycling charge, the availability of a flat fee yard waste service, and the resulting tremendous curbside recycling participation rate that has been achieved, King County claims that the rates established by the Commission "create a strong financial disincentive for customers to reduce waste and to recycle," and are insufficient to meet the waste reduction requirements of RCW 70.95.010. Complaint, p. 4-5. This allegation is absurd. Eastside's current cost-based variable can rates obviously do provide a financial benefit to customers who reduce their waste output and lower their service level. King County's complaint is actually that the Commission should adopt rates which might force customers to reduce or recycle a higher percentage of their waste.

The Waste Not Washington Act does not state how the Commission must set rates. Nor does it in any way revoke the Commission's authority. To read such limits into the statute would be completely inappropriate. When there is no showing of ambiguity, the meaning of a statute is derived from its plain language alone. Geschwind v. Flanagan, 121 Wn.2d 833, 840, 854 P.2d 1061 (1993). "In interpreting a statute, the court should assume that the Legislature meant exactly what it said." Id. at 841; citing, King County v. Taxpayers of King County, 104 Wn.2d 1, 5, 700 P.2d 1143 (1985). The case put on by King County is perhaps the best illustration of the clarity of the statute. The County was unable to demonstrate any actual ambiguity in the statute. In addition, the County made no attempt to state what rate structure, and what rate schedule, are required by RCW 70.95.010.³

King County has adopted an ordinance which states that the County preference is a rate spread of sixty percent between the mini and one-can rates, forty percent between the one and two-can rates, and twenty-five percent between the two and three-can rates.

³ King County witness Hanson seems to believe that his opinion of the meaning of RCW 70.95.010 should be given special weight, since he "participated in the drafting of the Waste Not Washington Act, including the legislative findings." Ex. T-RGH, p. 31. Many groups, including the solid waste haulers' association, the Commission, and various local governments participated in the drafting of the Act. In interpreting the meaning of a statute, however, even the opinion of an individual legislator is considered inadequate to establish legislative intent. In re F.D. Processing, Inc., 119 Wn.2d 452, 461, 832 P.2d 1303 (1992). The value of Mr. Hanson's opinion certainly falls far short of the value of a legislator's.

KCC 10.18.020. The ordinance does not state that the Commission is required to use this rate structure. The County has not provided any evidence to show that this rate structure would result in rates which are fair, just, reasonable and sufficient. In deciding on this rate spread, the County did not perform any type of cost analysis. Nor did it study the effects various rate structures might have on the behavior of Eastside's customers. Rodney Hanson described the decision as what he would call more of a "policy type compromise than the result of any specific analysis that if we make a 60 percent differential, we're going to get a certain impact." Tr. 102.

If there is any violation of RCW 70.95.010 to be found, it is in the arbitrary rate spread supported by King County. Under the rate structure approved by the Commission for Eastside, the percentage of difference between the rates at each service level increases as the number of cans used increases. This places the strongest financial burden on the two and three can users. In sharp contrast, King County seeks to impose a tremendous sixty percent penalty on the customer that uses one can instead of the mini can, but only increase the rate by twenty-five percent if a customer increases his subscription level from two to three cans.

RCW 70.95.010 seeks to encourage waste reduction and recycling. As King County witness Pealy agreed, a family that has reduced its waste output to one can is doing "a pretty darn good job" of recycling. Tr. 379. Even when Eastside had a sixty

percent differential between the mini and one can rates, less than five percent of the Company's customers were able to use just a mini can. Tr. 264-265. It would be pointless to excessively penalize one can customers who are already making an admirable attempt to reduce and recycle their waste. It is far more likely that the family using two or three cans could be persuaded to increase its recycling efforts.

2. The Commission set Eastside's rates in a manner consistent with RCW 81.77.030.

The Waste Not Washington Act also amended RCW 81.77.030, which sets forth the Commission's duty to establish solid waste collection rates. As amended, that statute states, in relevant part:

The commission shall supervise and regulate every solid waste collection company in this state,

- (1) By fixing and altering its rates, charges, classifications, rules and regulations;
- (2) By regulating the accounts, service, and safety of operations;
- (3) By requiring the filing of annual and other reports and data;
- (4) By supervising and regulating such persons or companies in all matters affecting the relationship between them and the public which they serve;
- (5) By requiring compliance with local solid waste management plans and related implementation ordinances;

(6) By requiring certificate holders under chapter 81.77 RCW to use rate structures and billing systems consistent with the solid waste management priorities set forth under RCW 70.95.010 and the minimum levels of solid waste collection and recycling services pursuant to local comprehensive solid waste management plans. The commission may order consolidated billing and provide for reasonable and necessary expenses to be paid to the administering company if more than one certificate is granted in an area.

King County claims that the Commission was required by RCW 81.77.030(5) to adopt rates that are consistent with the County's solid waste management plan and related ordinances. Complaint at 3. The Staff agrees that the Commission is required to, and has, set rates consistent with the solid waste management plan and related ordinances. However, the scope of King County's plan, and its ordinances, extend far beyond the bounds of King County's jurisdictional authority. The Commission is not required to implement portions of the County's plan, or ordinances, which exceed the County's authority.

In RCW 70.95.090, the Legislature provides a very specific list of the elements which must be included in solid waste management plans. At no point in this statute is the County given authority to set rates, or to require the carrier to request specific rates from the Commission. King County appears to believe that it has this authority under RCW 70.95.90(6)(a) and (b), which state that the County must provide programs that reduce waste and provide an incentive to recycle.

This argument is insupportable for two reasons. First, it would obviously be an improper reading of the plain language of the statute to interpret the language regarding incentive "programs" to mean that the County has the option to usurp the Commission's authority to set rates. Statutes must be construed to effect their purpose, and unlikely, strained or absurd results must be avoided. Cherry v. Seattle, 116 Wn.2d 794, 802, 808 P.2d 746 (1991). If King County's reading of the statute were adopted, the scope of the County's authority would be limitless. The logical extension of the County's reasoning would be to find that the County also has the power to shape "programs" by granting and revoking permits. Such a reading would obviously be an inappropriately strained interpretation of the statute.

The second reason that King County's reading of the statute is flawed is that the Legislature very carefully articulated exactly what elements the solid waste plans will contain. King County lacks the authority to expand upon that explicit list. The Supreme Court of Washington has found:

Where a statute specifically designates the things or classes of things upon which it operates, an inference arises in law that all things or classes of things omitted from it were intentionally omitted by the legislature under the maxim *expressio unius est exclusio alterius* - specific inclusions exclude implication.

Washington Natural Gas Co. v. Public Util. Dist. No. 1 of Snohomish County, 77 Wn.2d 94, 98, 459 P.2d 633 (1969), citing State v. Roadhs, 71 Wn.2d 705, 707, 430 P.2d 586 (1967). The Legislature has specifically set forth a detailed list of what the County has

authority to include in its plan. There is nothing in the statute to even hint at legislative intent to allow counties to impair the Commission's authority to set rates.

The Legislature has given counties two limited types of rate authority. The first is the power to set rates at solid waste disposal facilities. RCW 36.58.040. In RCW 36.58.040, the Legislature specifically stated that "[n]othing in this section [RCW 36.58.040] shall be construed to authorize the operation of a solid waste collection system by counties or to authorize counties to affect the authority of the utilities and transportation commission under RCW 81.77.020." The only other time a county may control rates is when the county exercises its option to enter a contract for collection of recyclable materials. Although the Legislature created an exemption from chapter 81.77 RCW for solid waste carriers operating under a contract with any city or town, and for cities and towns which undertake solid waste disposal, the Legislature did not allow counties to control solid waste collection.

Since the County is without authority to include rate provisions in its solid waste management plan, King County's local ordinance dictating that haulers file rates pursuant to the rate structure the County wants, and urging the Commission to adopt such rates, cannot be considered an ordinance which implements the plan. Therefore, Eastside was not required to file rates in compliance with the portion of King County's ordinance dictating rate spreads,

and the Commission was under no obligation to accept the rate structure proposed in the ordinance.

3. The County has not shown that adoption of the rate spread it favors would create a significant increase in waste reduction and recycling.

King County claims that if its proposed sixty, forty, twenty-five percent rate spread is adopted, it will result in increased waste reduction and recycling. It is important to note that the Staff agrees that variable can rates are appropriate, and that they are one factor which encourages the public to reduce and recycle waste. The rates the Commission has approved for Eastside are variable can rates, which are set based on the cost of providing service. This simultaneously accomplishes the goal of providing fair, just, reasonable, and sufficient rates, and the Waste Not Washington Act's goal of providing an incentive to reduce and recycle waste. However, King County has not provided any evidence to establish that increasing the existing variable between the service level rates will result in increased recycling. As was stated by Staff witness Popoff, the evidence presented by King County's witnesses actually suggests that the steeply inclining rate design favored by the County "could have only a minimal impact on waste reduction and recycling, relative to cost-based variable rates, and . . . the effect will diminish over time." Ex. T-101, p. 14.

The County's witnesses presented a scattered range of elasticity estimates, from a high of -0.2 to low of -0.07.⁴ Ex. T-58, p. 8; Ex. T-49, p. 8. By the County's own admission, a **one hundred percent** increase in the rates may result in as little as a **seven percent** decrease in the solid waste stream. This modest end does not justify the draconian means that the County is advocating.

King County witnesses Albert and Skumatz made broad brush estimates of the general relationship between the rates for solid waste and recyclables collection and the amount of waste which can be diverted from the landfill. However, neither Dr. Albert nor Dr. Skumatz attempted to distinguish the effect of the incentive produced by the cost-based variable rates currently in place, from the effect the rate structure proposed by King County would have.

King County witness Albert presented an elasticity estimate based on the price difference between one and two can service. Ex. T-58, p. 5. However, Dr. Albert also admitted that the quantity of waste that was used in the model included waste from all service levels, from the mini can level to the four can level. Tr. 396. Therefore, reductions in waste from mini can, one can, three can, and four can customers were all ascribed to the change in the rate between one and two can service. This caused Dr. Albert's estimate to overstate the sensitivity of the elasticity of demand.

⁴ As Mr. Popoff explained, elasticities between -1 and zero are considered inelastic. Ex. T-PJP, 12. The quantity response is weaker than the price change. This does not mean there will not be any change in behavior. Rather, it means that any change that does occur will be very small or insignificant.

The testimony of King County witness Skumatz calls Dr. Albert's broad conclusion into further question. Dr. Skumatz's article, entitled "Variable Rates in Solid Waste", suggests that customers are less likely to switch from one-can service to mini-can service than they are to switch from two-can service to one-can service. Ex. 70. Dr. Skumatz's article provides two reasons to believe that elasticity decreases at lower service levels. First, one-can customers have fewer lower subscription levels available to them. Second, the percentage of waste that would need to be recycled would be much higher. See id. at III.42. Therefore, it would be improper to view Dr. Albert's limited study of the elasticity of demand between two and one-can service as a statement of elasticity at all service levels.

The utility of Dr. Albert's simplistic study is further hampered by its misspecification bias that all behavior changes are due to a change in the price.⁵ Yet King County obviously believes that a significant change in customer behavior is gained through educational programs. In fact, the County is so confident of this that it will spend nearly one million dollars in 1994 to change behavior through advertising and education. Tr. 425; Ex. 100. As Mr. Popoff explained in his testimony, price is not the only factor

⁵ The biases in Dr. Albert's elasticity estimate are not surprising. According to Dr. Albert, her model was not developed to estimate demand elasticities. The purpose of the model was to identify differences in recycling and disposal between suburban cities and unincorporated King County in 1992. Tr. 394; Ex. 59, p. 3.

that influences people's behavior. In addition to reacting to price, "customers seek to maximize what they consider to be their own well-being." Ex. T-101, p. 3. By spending nearly a million dollars on advertising and public education, the County is persuading consumers that it is their moral duty to perform distasteful chores, such as scraping labels off containers and cleaning dog food cans, so that they can help save the environment. An excellent illustration of the inward shift in demand that education can cause is provided in Exhibit 103.

Dr. Skumatz's estimate of elasticity is even more deeply flawed than Dr. Albert's. In support of her elasticity estimate of $-.09\%$ to -0.14% , Dr. Skumatz referred to programs throughout the country that have achieved dramatic increases in waste diversion after implementing an incentive rate structure, and instructed the Commission that similar results could be achieved if Eastside's rates are changed. Ex. T-65, p. 13. In delivering this lesson, Dr. Skumatz withheld the fact that most of these rate structures were put into place at the very same time that curbside recycling was first introduced. Tr. 484-491. Perhaps the most striking misuse of the data was Dr. Skumatz's reliance on waste diversion in Oakland, California. Oakland had a flat rate for the collection of an unlimited quantity of solid waste. During the time that the flat rate was in effect, residents voluntarily diverted thirteen percent of their waste. Tr. 489; Ex. 100, Resp. to Data Req. 14. When a city wide curbside recycling program was implemented, and a

variable rate structure was introduced, the waste diversion rate increased to thirty percent. Id. As explained in Mr. Popoff's testimony, the introduction of a convenient substitute will effect people's preferences. Ex. T-101, p. 8. Although customers' behavior is obviously greatly influenced by the newly available option to use curbside recycling, Dr. Skumatz made absolutely no effort to calculate the impact of this critical variable.⁶

In her rebuttal testimony, Dr. Skumatz endeavored to remedy the flaw in her reasoning by pointing out that twenty-four percent of Seattle's tonnage was recycled after the introduction of incentive variable can rates, and before the implementation of convenient curbside programs. Ex. T-73, p. 6. Once again, Dr. Skumatz attempted to mislead the Commission by telling only half of the story. As Mr. Pealy explained, prior to introducing variable can rates, Seattle residents only had two options. Either they could use a 120 gallon container (a four can equivalent) supplied by the city, or they could purchase their own can and receive single-can service. Tr. 320-321. Although the difference in volume was tremendous, the difference in price between the two

⁶ The testimony of King County witness Gaisford was similarly flawed. Mr. Gaisford concluded that the waste reduction experience by Bellevue, Lake Forest Park, and Mercer Island was attributable to the customers' response to rate changes. Ex. T-29, p. 7-8. During cross examination, Mr. Gaisford admitted that the rate changes occurred at the same time that curbside recycling was first introduced. Tr. 245. In addition, Mr. Gaisford revealed that he had no idea whether the cities' rate changes effected the percentage differential between the rates for each service level. Tr. 246.

services was only \$1.50. Tr. 322. As a result, eighty-two percent of Seattle residents used the 120-gallon service. Tr. 320. Not surprisingly, when Seattle gave residents the option of saving money by subscribing to intermediate levels of service, such as two or three-can service, many of them changed their service level.

Dr. Skumatz also attempted to use Seattle's garbage by the pound study to bolster her argument for the rate spread King County is seeking. She attempted to assert that changing from a variable can market structure to garbage by the pound resulted in a reduction in waste, and that therefore, the Commission should increase rate differentials. This argument is little more than an attempt to win the argument by confusing the issues. Garbage by the pound is not a rate structure. It is a market structure. Using a garbage by the pound market structure would enable the Commission to establish the most accurate, honest, cost-based rates possible. For that reason, the Staff strongly supports a garbage by the pound market structure, and is hopeful that it will become feasible in the near future. But the outcome of the garbage by the pound market structure experiment cannot be used to estimate how alterations in the rates used in a variable rate structure would impact behavior. This is a comparison of apples and oranges.

Like Dr. Albert, Dr. Skumatz also chose to ignore the impact of public education and advertising. Without knowing to what extent changes in behavior are due to the impact that is made on the public's preferences through advertising and education, and

offering convenient alternatives such as curbside recycling, it is impossible to state what portion of the elasticity of demand is attributable to variations in price. Ex. T-101, p. 21-23. A properly calculated elasticity of demand would isolate the effect of price. Id. at 22. Rather than correcting this error, Dr. Skumatz used her rebuttal testimony to state that the Staff hadn't established to what extent residents' preferences, and the availability of curbside recycling, affect consumers' behavior. Ex. T-73, p. 3, 9-13. Throughout this case King County has failed to understand that as the complainant, they bear the burden of proof. It is frankly astonishing that Dr. Skumatz submitted an incomplete and erroneous study with the expectation that the Staff would correct her work for her.

King County's assertion that Mr. Popoff's testimony should be dismissed because it addresses the impact of changing preferences further calls into question the credibility of the County's economists. Economists would be ill-equipped to design an education campaign to change preferences. They would not be the appropriate experts to consult in determining where advertisements should be placed, or how a program to educate children should be designed. However, economists are concerned with the change in preferences that advertisements and education cause, and the impacts the change in preferences has on demand functions. As Mr. Popoff pointed out, how changes in preferences affect demand functions is not an issue that is examined rigorously in graduate

level economics texts, because preference is treated as a given, so that it is one less variable that must be addressed. Tr. 868. The purpose of King County's complaint, however, is not to explore economic theories. King County claims that it is capable of predicting customer reaction to the price of service. In order to make this prediction, the impact of price must be isolated from all other factors that influence the public's behavior. Since King County believes that advertising and education have a substantial impact on the public's behavior, the County's witnesses should have considered to what degree changes in behavior are attributable to King County's million dollar education and advertising campaign. Although King County's economists were able to construct complex econometric models, they failed in their analyses to observe basic principles of microeconomics and remove a very obvious bias.

As a final testament to the reliability of King County's elasticity estimates, consider Dr. Skumatz's failure to recognize that it is highly likely that the demand elasticities will become less elastic over time. As individuals respond to a variable rate structure and public education by reducing and recycling their waste, it will become increasingly difficult for them to find ways to increase their recycling efforts. Ex. T-101, p. 25. King County witness Pealy stated that the City of Seattle has experienced a fifty percent decrease in elasticity over the last four years. Mr. Pealy stated that:

[G]iven the high curbside recycling participation rate in Seattle, and our high recovery rates, we would expect this elasticity to decline over time. High recovery rates [of recyclable material] means that less recyclable material remains in the garbage stream, so the rate increases produce smaller and smaller increases in recovery rates over time.

Ex. T-49, p. 9. Since Eastside's residents have had inclining, variable rates, curbside recycling, and yard waste service available to them for a number of years, the elasticity of demand in Eastside's service territory is likely to have become much more inelastic than it was when the curbside collection and yard waste programs were first introduced. Ex. T-101, p. 26-27.

King County simply has not provided any studies which would justify the abandonment of cost-based rates. None of the estimates provided by the County of the elasticity of demand indicate how customers would respond to the rate structure King County supports. There has been absolutely no attempt to isolate the effect of price on consumers' behavior. And the County's economists have refused to admit the obvious fact that elasticity will decline over time. Given King County's failure to even attempt to meet its burden of proof, the Commission should continue to employ a rational, effective, cost-based variable rate structure.

B. The Commission Set Rates for Eastside's Customers Which Are Properly Tied to the Company's Actual Cost of Providing Service.

The rates the Commission established for Eastside were carefully calculated to reflect the actual cost of providing service to various classes of customers. Since 1961, this Commission has used its considerable expertise, and the assistance

of a solid waste staff comprised of highly competent regulatory accountants and economists, to set rates which are fair, just, reasonable and sufficient.

The present rate-setting method employed by the Commission has been refined over time. Historically, the Commission has regulated solid waste rates through the use of a fixed ninety-three to ninety-four percent operating ratio. In 1988, the methodology was adjusted to permit the Commission to determine carriers' revenue requirement on a variable percentage, and consider each carriers' rate base, tax rate, revenues, and expenses. In re Consolidated Garbage Cases, Cause No. TG-2016 et al. (1988). As part of its order, the Commission stated that it expected to receive solid waste cost of service studies from large carriers. In 1991, the Commission took further steps to ensure that the rates would be even more closely related to the actual costs incurred by each carrier, by considering each carrier's capital structure and cost of debt. Ex. T-88, p. 3-4.

1. The Staff properly examined Eastside's revenue, expenses, and cost of service in recommending rates to the Commission

a. Solid waste rates

The solid waste and yard waste rates for Eastside Disposal were properly set using the methodology outlined above. When Eastside filed for a rate increase, Staff accountant Layne Demas audited the Company's books and records to determine the Company's actual expenses, revenue, investment and cost of service during the test year which ended June 30, 1993. By using an historical test

year, the Staff was able to audit the Company's books, determine which expenses are just and reasonable, and ensure that only used and useful property is contained in the rate base.

Mr. Demas prepared a work sheet detailing the specific revenues and expenses, and updated the test year by making pro forma and restating adjustments to reflect changes in the next year which are currently known, measurable, and not offset by other factors. Ex. 96, p. 3-6. None of the adjustments were contested by King County. In fact, it appeared during the case that the County did not even attempt to understand how or why the Commission makes adjustments to the test year.

After calculating the Company's total cost of service, Mr. Demas examined the cost of service study filed by Eastside. The purpose of a cost of service study is to determine the cost of each type of solid waste collection service provided by the Company. Ex. T-88, p. 3. The cost of labor, disposal fees, fuel, repairs, depreciation, overhead, taxes, equipment, and disposal fees are all considered, and "allocated to the various types of services offered in proportion to the resources consumed in the provision of that service." Id. In allocating these costs, Mr. Demas considered the time needed to provide each service, and the weight of the waste collected. Ex. T-95, p. 7.

As part of its cost of service study, Eastside provided a weight study, which was performed by collecting waste from fifty customers subscribing to the same service level, weighing the total

amount collected, and then dividing the total by fifty to determine the average weight. This was done at each service level. Ex. T-76, p. 7. Mr. Demas compared the results of Eastside's study to the Meeks can-weight study, which had previously been accepted by the Commission, and the can weights determined by other regulated carriers, to determine whether the weights fell within a zone of reasonableness.⁷ Tr. 727. The focus of his examination was not the actual weights themselves. Rather, the relevant factor was the percentage of difference in the weights between each service level. It is this percentage spread which is used to allocate costs between the service levels. Mr. Demas determined that there should be a twenty-four percent difference between the mini and one-can rates, a twenty-nine percent difference between the one and two-can rates, and a thirty-seven percent increase between the two and three-can rates.⁸

In her testimony, Dr. Skumatz appears to have completely misunderstood the purpose of determining the can weights. She

⁷ The Meeks can weights are now invariably higher than the can weights which are presently occurring, because the Meeks study was performed prior to the implementation of curbside recycling and yard waste collection programs. Tr. 713-714. As a result of curbside recycling and yard waste collection, large portions of heavy materials such as glass, newspapers, and grass clippings have been removed from the solid waste stream.

⁸ These are the percentage spreads between solid waste rates, not the combined rate for solid waste and curbside recycling collection. The solid waste rate must be considered separately when the rates adopted by the Commission are compared to the rate spread requested by the County. It is meaningless to compare Eastside's combined solid waste and recycling rate to the County's recommended solid waste rates.

stated that the weight spreads used by the Staff "do not appear to be stable or robust" and that one should question rates derived by using them. Ex. T-73, p. 4. Dr. Skumatz believes that more reliable weights were determined in Seattle's garbage by the pound study.⁹ Id. at 17-18. In reality, the weight spreads in the garbage by the pound study validate the reasonableness of Eastside's study. The percentage of difference between the weights at each service level are nearly identical to the percentage spreads found by Eastside. Ex. C-74; tr. 492-493. Using Dr. Skumatz's preferred can weights would have a negligible effect on Eastside's rates.

b. Yard waste collection rates

Yard waste collection rates are based on the total cost of providing yard waste service. The yard waste program is supported independently, by the customers that require the service. Yard waste rates are not subsidized by the solid waste rates. Many of Eastside's customers do not need the service, because they do not produce yard waste. According to King County witness Gaisford, forty to forty-five percent of Eastside's customers are currently composting some or all of their yard waste.¹⁰ Tr. 227. Many others either use a lawn care service which hauls away their yard

⁹ The County did not perform a study of can weights, or present estimated can weights. The only can weights provided by King County were the weights calculated in Seattle's garbage by the pound study. Tr. 405.

¹⁰ As a matter of policy, King County prefers that residents compost their yard waste. Tr. 201

debris, or do not have a yard. Ex. T-88, p. 22. Because of this, subscription to yard waste service is optional.

c. Curbside recycling rate

King County is not contesting the rates for curbside recycling service. As with the yard waste service, the rate for curbside recycling is not subsidized by the solid waste service. It is set based on the total cost of providing curbside recycling service.¹¹ However, unlike yard waste rates, curbside recycling is a mandatory charge. The reason for this is that, as stated above, not all customers generate yard waste. In contrast, virtually everyone has a need to discard recyclable material. Ex. T-88, p. 22.

2. King County has neglected to offer an alternative rate setting methodology, or rate schedule, that it believes is appropriate.

While the content and support of King County's complaint are troubling, what is even more troubling are the striking omissions. Although the County has complained against the rates adopted by the Commission, it has not provided an alternative rate-setting methodology or an alternative rate schedule. Rather than presenting a complete, coherent case, the County has inappropriately left the parties and the Commission to speculate as to what method of rate regulation the County is seeking, and then to respond to the legality of these inferences.

¹¹ Although all of Eastside's customers pay for recycling service, bins are not delivered unless the customer requests them. This reduces the overall cost of the recycling program, and translates into a lower recycling charge for all customers.

a. Solid waste rates

The County claims that the solid waste rates should be set with a sixty percent increase between the mini and one-can rates, a forty percent increase between the one and two-can rates, and a twenty-five percent increase between the two and three-can rates.¹² Ex. T-1, p. 18-19. However, at no point during the proceedings was King County willing to state how rates should be set to meet this goal.

1) Rate setting methodology

With respect to a rate setting methodology, Dr. Skumatz made an extremely brief statement in her rebuttal testimony that she believes the Commission should employ long run marginal cost pricing. Ex. T-73, p. 22. After introducing this terminology, Dr. Skumatz made absolutely no effort to explain the economic theory, or state how the abstract theory could possibly be applied to set solid waste rates.

Long run marginal cost pricing is usually referred to as long run incremental cost pricing (LRIC). LRIC pricing considers the future cost of service, rather than limiting the examination to the cost of serving existing customers. This has caused some economists to question the use of LRIC pricing. For example, William Melody has stated:

¹² This is the rate spread recommended in KCC 10.18.020. Although the County endorses this rate spread, the ordinance does not attempt to order the Commission to establish rates consistent with the ordinance.

The framework for marginal cost analysis assumes a planning horizon sufficiently distant that all the effects of all alternative decision possibilities can be taken into account. But all of this information is hypothetical and subject to the forecasting ability of the decision maker . . . As a practical matter we know in advance that our hypothesis of optimization will be disproved by reality.

Melody, "The Marginal Utility of Marginal Analysis in Public Policy Formulation," Journal of Economic Issues 8 (1974): 295.

Three threshold issues need to be addressed when LRIC is used. First, the proper time frame must be determined. The focus must be on the cost of providing service over a set number of years into the future. Over that period of time, an estimate must be made of future expenses. Dr. Skumatz did not state what time period the County would propose using. Without knowing the time frame that is being proposed, it is impossible for the Staff and the Company to estimate the future expenses.

The second issue which must be addressed if LRIC rates are to be set is the calculation of what the incremental (or marginal) costs will be over time. In this case, the primary variable component of the rates is the disposal fee at King County's Cedar Hills Landfill. Ex. T-88, p. 3. Although King County is in the best position to make this estimate over time, Dr. Skumatz did not make any attempt to do so. After admitting that applying LRIC rates would be complicated by the fact that King County's disposal rates may not currently reflect long term costs, Dr. Skumatz made no effort to calculate the costs. Ex. T-73, p. 22. Perhaps Dr. Skumatz recognized that it is quite possible that increased future

costs will be offset by disposal cost savings. The United States Supreme Court recently found that a flow control ordinance similar to King County's was unlawful. C & A Carbone, Inc. v. Town of Clarkstown, __ U.S. __, 128 L. Ed. 2d, 114 S. Ct. 1677 (1994). In the near future, Eastside may be able to substantially decrease its disposal costs by using a different landfill.

The third issue which must be addressed is designing LRIC rates that are tied to Eastside's revenue requirement. By definition, LRIC rates are based on an estimate of what will occur in the future, rather than on the actual costs incurred by the regulated company. Dr. Skumatz recognized that if the rates are not closely related to the revenue requirement, an over or under recovery will occur. Ex. T-73, p. 22. Her solution was a suggestion that the Commission use "balancing accounts", and adjust for any over or under collection by making a retroactive adjustment in the next case. Ex. T-65, p. 4; tr. 482. As this Commission is well aware, retroactive ratemaking is not appropriate. If balancing accounts were employed, residents that become Eastside customers at a later date could be unfairly penalized by a rate which is higher than the cost of service, in order to compensate the Company for the low rates enjoyed by previous customers. For this reason, retroactive ratemaking has historically been rejected by the courts. See Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571, 578, 69 L.Ed.2d 856, 101 S. Ct. 2925 (1981).

In support of King County's argument that an LRIC rate setting

method should be employed, Dr. Skumatz states that LRIC based rates have been implemented by this Commission for electric and telecommunications companies. The Staff can only assume that Dr. Skumatz did not take the time to read the Commission's orders before attempting to summarize them. The Commission does not use an LRIC rate setting method for electric companies. It is possible that the County misunderstood another type of rate structure used by the Commission. The Commission sets simple inclining tail block rates for Puget Power's residential customers. The rate for the first block reflects the base load cost of hydroelectric power. A higher rate is set for the next block, which reflects the incremental cost of obtaining power from other sources. Washington Util. & Transp. Comm'n v. Puget Sound Power and Light, Docket Nos. UE-920433 et al., p. 97 (Eleventh Supp. Order, 1993). These rates are not set using an LRIC method. Rather, they are based on a determination of the historical cost of obtaining power from various sources.¹³ Id.

The Commission does use LRIC in setting competitive telecommunications rates. The reason for this is that in response to competition and rapid technological changes, companies' revenue requirements are rapidly changing. LRIC rates are appropriate only because of the competition which exists in the telecommunications

¹³ Although the inclining tail block rates the Commission has approved for Puget may encourage conservation, these rates are in no way comparable to the arbitrary rate spreads King County seeks. The price for electricity is based on the actual historic cost of providing service with different power sources.

industry. In sharp contrast, Eastside has a monopoly, and a comparatively stable capital structure. It should be noted that even in using LRIC pricing for competitive telecommunication services, the Commission only looks forward for a very limited period of time. The Commission has not completely abandoned financial reality in favor of hypothetical capital structures which may come into existence in the distant future.

2) Rate structure

Despite the apparent conflict with Dr. Skumatz's belief that LRIC pricing methods should be used, King County's witnesses repeatedly stated that setting cost-based rates, with the revenue requirement found by the Commission, is appropriate. Apparently the County would approve of rates set using the revenue requirement as a ceiling, with a sixty percent increase between the mini and one-can rates, a forty percent increase between the one and two-can rates, and a twenty-five percent increase between the two and three-can rates.¹⁴ At no point during the proceedings, however, was King County willing to state how rates could be set to meet this goal.

The Staff can speculate as to only two ways the County's proposed rate spread could be reflected in a rate design. The first is to price the mini-can at the cost of providing the service, the one-can rate sixty percent higher than the mini can

¹⁴ Although the County endorses this rate spread, the ordinance does not attempt to order the Commission to establish rates consistent with the ordinance.

rate, the two-can rate forty percent higher than the one-can rate, and the three-can rate twenty-five percent higher than the two-can rate. This would result in a ridiculous over recovery of Eastside's revenue requirement. With the exception of the mini can rate, each service would be obscenely over priced. The result would be a windfall profit for Eastside, at the expense of the public.

The second is to set a mini can rate which is priced below the cost of service, and to subsidize the mini can rate by charging customers at other service levels a rate that exceeds the cost of service. This would unfairly penalize customers at all other rate levels. King County believes that mini can customers should be rewarded for their recycling efforts, and that penalizing customers at other service levels by requiring them to subsidize the mini-can rate will cause them to reduce their waste output. This argument is completely baseless. King County has made absolutely no attempt to prove that mini can customers are recycling a higher percentage of their waste. Obviously, homes with a single occupant, such as a student, a bachelor, or a senior citizen, would be expected to produce far less waste than homes containing families. If a single person subscribes to a mini can, there is no reason to believe that the individual is recycling a larger percentage of his or her waste than is being recycled by a family that subscribes to one or two-can service. The City of Seattle has recognized that if a family has reduced its service level to one can, it has probably done a

very good job of recycling. Tr. 379. In recognition of this fact, even under Seattle's extremely aggressive incentive rate design, rates do not begin to sharply increase until the two-can service level. Id.

The Commission should maintain Eastside's present rate design, and recognize that mini can users are not the only residents that are making a concerted effort to reduce and recycle. Certainly, there are extraordinary families that are able to compress their waste into a mini can. It is doubtful, however, that the majority of families could reduce their waste output to that degree. As both Mr. Popoff and Mr. Pealy have noted, the demand curve becomes increasingly inelastic over time, as people reach a point at which they have reduced their waste as much as they are capable of doing. It would be both unfair and unproductive to penalize people who are already doing their best to recycle.

b. Yard waste rates

King County would like the Commission to set a lower yard waste rate. As with the solid waste rates, King County did not provide any manner in which this might be accomplished. King County's primary policy witness, Mr. Hanson, did indicate that the County believes that the yard waste program should remain voluntary. Tr. 177. Mr. Hanson also agreed with the Commission's position that customers should not be required to pay for yard waste service unless they actually receive it. Tr. 177.

There are only two possible ways of lowering the yard waste

rate. The first is to deliberately set the rate below the cost of providing the service. This would make it impossible for Eastside to collect the cost of providing the service, and would constitute an illegal, confiscatory rate. The Commission does not have authority to order a regulated carrier to donate services to the public. POWER v. Washington Util. & Transp. Comm'n, 104 Wn.2d 798, 808, 711 P.2d 319 (1985). The second possible method would be to price yard waste below the cost of service, and force all solid waste customers to subsidize the yard waste rate. This method directly conflicts with King County's testimony that customers that do not subscribe to yard waste service should not be required to pay for it. Tr. 177. Customers that go to the additional effort of composting their waste, pay a yard service to haul their yard waste away, or who have eliminated their yards, should not be penalized by a solid waste rate that forces them to subsidize yard waste service.

In reality of course, if rates were approved which required solid waste customers to subsidize yard waste rates, the public would probably never even realize what was happening. It is King County's position that billing statements should not inform consumers of the cost of the individual services they are receiving. Customers pay a combined total for solid waste, yard waste, and recycling services without being told the price of the individual services. Ex. T-88, p. 13-14.

C. There Are Many Ways King County Can Further Its Recycling Goals Without Resorting to an Unfair Rate Structure.

Under RCW 70.95.090(6), King County is required to include in its comprehensive plan:

A comprehensive waste reduction and recycling element that, in accordance with the priorities established in RCW 70.95.010, provides programs that (a) reduce the amount of waste generated, (b) provide incentives and mechanisms for source separation, and (c) establish recycling opportunities for the source separated waste.

Despite these requirements, King County has not explored any new means of encouraging recycling, other than attempting to force the Commission to change Eastside's rates. Tr. 113. There are a number of potentially highly effective options the County should consider exercising before seeking to burden the County's residents with unfair rates.

The first option the County could pursue is to listen to the testimony of Dr. Skumatz and include the cost of environmental externalities in the disposal rate at the Cedar Hills landfill. As stated above, all of the externalities Dr. Skumatz considered to be noteworthy are directly related to the cost of the operation and closure of the landfill. If the disposal fee was increased to reflect the externalities, the increase would flow through to Eastside's customers and result in universally higher rates. RCW 81.77.160(1). According to King County witness Pealy, increasing the overall rate levels could have the same effect as having a more steeply inclining rate structure. Tr. 361. Of course, increasing the landfill rate may have political repercussions. The residents of King County just might realize that the County was responsible for the rate increase.

Another method King County could employ to increase participation in the curbside recycling program is to institute a penalty for customers that do not set out recyclable materials for collection. This is currently being done in Pierce and Thurston Counties. If the carrier sees that the customer has not placed any recyclable materials at curbside, the customer is assessed a penalty charge. The penalty is not charged if the customer takes his or her recyclable materials to a buy-back center, or gives them to a charitable organization. Since King County believes that the most effective way to change behavior is through a monetary punishment, this should be an attractive option to the County.

A penalty provision could also be used to enforce King County's yard waste ordinance. It appears that the County has not made any effort to penalize residents that violate the ban on putting yard waste into the solid waste stream. If there are any residents that are violating the ordinance, knowledge that King County intends to enforce the ban would give them a strong incentive to comply with the law.

King County could expand the service level options to include the micro can.¹⁵ This is an option that other counties have put into place. It gives small or single person households an incentive to further reduce and recycle their waste. This option may appeal to a number of the King County residents that spoke at

¹⁵ A micro can is usually defined as ten gallons or less. In contrast, an mini can is twenty gallons or less.

the public hearing. It would give them a greater financial reward for their recycling efforts.

King County could also encourage public participation in the waste reduction and recycling program by supporting a billing system that sends county residents a clear, and honest message about the price of the services they are receiving. King County has long supported a billing system that only shows the customer the total price for all services. Customers are not told the specific cost of solid waste, curbside recycling, and yard waste collection. The confusion that this billing system causes was made painfully apparent during the public hearing. For example, one customer stated that his mini can rate had been increased to \$9.65. Tr. 784. He then compared this to solid waste rates charged in other cities. The customer obviously did not understand that the rate for the mini can is actually \$5.21, and that recycling is an additional \$4.44. Nor did he appear to understand that the rate for curbside recycling had been increased. This confusion was shared by other residents. Tr. 819, 826, 832. As Staff witness Colbo stated, "[w]ith total disclosure, the impact of an unlimited-use service (recycling) versus an increasingly expensive service based on usage (garbage) would be more visible and effective. Having them embedded together hides these facts from the consumer." Ex. T-88, p. 14.

King County also has the ability to keep the landfill open. The County has vehemently protested the impact it believes

Eastside's current rates will have on the life of the landfill. Yet, King County has made a political decision to close the landfill three years earlier than it was originally slated to close. Tr. 106, 160-161. According to Mr. Hanson, the County weighed the desire of residents to have a larger "buffer zone" against the County's plans for development, and decided to shorten the landfill's life. Id. After making this policy decision, it is absolutely inappropriate for King County to argue that Cedar Hills Landfill is so valuable that it justifies charging the public inflated solid waste rates. If the County believes that the landfill is a highly valuable, irreplaceable site, it should make the tough political decision of allowing development of the landfill to continue.

Finally, King County can assume control of the regulation of residential curbside recycling rates. RCW 81.77.130; (see footnote 1). The Waste Not Washington Act does not permit counties to dictate to the Commission what rates it must set. If a county disagrees with the rate-setting methodology used by the Commission, the county can assume complete control of the regulation of residential recyclable materials collection. With a four hundred person staff, and an annual budget of \$59,712,000, the County certainly has the financial resources to determine how it can regulate the carrier. Tr. 258; Ex. 2, p. 20.

III. CONCLUSION

The rates the Commission has established for Eastside accomplish the waste reduction and recycling goals set forth in the Waste Not Washington Act, while providing the public with fair, cost-based rates. The cost-based variable rate structure provides a financial incentive to customers to reduce their waste and subscribe to a less expensive service level. An outstanding level of participation has been achieved by Eastside in its curbside recycling program. Since the Commission is continuing to provide customers a rate incentive to decrease waste, there is no reason to believe that this will change.

King County has not met its burden in this case. The County has not established that the Commission failed to fulfill any of its statutory duties in establishing rates for Eastside. The County's sole objective appears to be to convince the Commission that it should abandoned Eastside's current cost-based variable rate structure, and arbitrarily impose the rate differentials supported by King County. The County has not offered any evidence to show that abandoning cost-based variable rates will increase waste reduction and recycling. King County should give serious consideration to some or all of the numerous means it has of encouraging waste reduction and recycling, before advocating a rate structure which sends inaccurate, and unfair price signals to the County's residents.

The Commission Staff respectfully requests that the Commission retain Eastside's present rate structure.

Respectfully submitted this 15th day of August 1994.

CHRISTINE O. GREGOIRE
Attorney General



ANNE E. EGELER
Assistant Attorney General

CERTIFICATE OF SERVICE

I hereby certify that I have this day served one copy of the following document upon Mary F. Perry, Senior Deputy Prosecuting Attorney, E550 King County Courthouse, 516 Third Avenue, Seattle, Washington, 98104-2390; and Elizabeth Thomas, Attorney at Law, 5400 Columbia Sea-First Center, 701 Fifth Avenue, Seattle, Washington 98104-7011, via U.S. Mail postage pre-paid.



ANNE E. EGELER

Dated: August 15, 1994