



# City of Northfield, Minnesota City Council Updates

Franchise Fee Review

October 13, 2020



# Goals and Outcomes for Work Session

- I. Review legal opinion regarding franchise fee implementation
- II. Updated Scenario: Flat Fee by *broad* customer classes
- III. Potential inequities from a flat fee approach
- IV. Potential Solution: Flat Fee based on more specific customer classes.
- V. Background on options (previously presented)
- VI. Obtain Council direction



# Legal Opinion on Franchise Fee Implementation

- Working assumption that the City had broad authority to impose franchise fee based on an implementation method of its choosing, i.e. flat monthly fee; % of revenue; % of usage, etc.
- The City obtained a legal opinion from Flaherty Hood P.A. that the existing franchise agreement from December 2012 stated that any future franchise fee:

*“shall be a flat fee per customer based on metered service to retail customers within the City or on some other similar basis.”*

- Result is the City cannot impose a fee based on a percent of usage without the consent of Xcel Energy, which is unlikely.

## Updated Scenario: Flat Fee by *broad* customer classes

|                               | Approx # of Premises | Option 1             | Option 2             | Option 3               |
|-------------------------------|----------------------|----------------------|----------------------|------------------------|
| <b>% Equivalent</b>           |                      | <b>3%</b>            | <b>4%</b>            | <b>5%</b>              |
| <b>Electric</b>               |                      |                      |                      |                        |
| Residential                   | 6,527                | \$ 2.50              | \$ 3.25              | \$ 4.00                |
| Small C&I: Non-Demand         | 485                  | \$ 3.00              | \$ 4.00              | \$ 5.00                |
| Small C&I: Demand             | 225                  | \$ 24.25             | \$ 32.50             | \$ 40.25               |
| Large C&I                     | 55                   | \$ 740.00            | \$ 990.00            | \$ 1,235.00            |
| Public Street Lighting        | 11                   | \$ -                 | \$ -                 | \$ -                   |
| Municipal Pumping: Non-Demand | 1                    | \$ -                 | \$ -                 | \$ -                   |
| Municipal Pumping: Demand     | 0                    | \$ -                 | \$ -                 | \$ -                   |
| <b>Total</b>                  | <b>7,304</b>         | <b>\$ 724,000.00</b> | <b>\$ 960,000.00</b> | <b>\$ 1,193,000.00</b> |
| <b>% Equivalent</b>           |                      | <b>3%</b>            | <b>4%</b>            | <b>5%</b>              |
| <b>Gas</b>                    |                      |                      |                      |                        |
| Residential                   | 5,265                | \$ 1.25              | \$ 1.75              | \$ 2.25                |
| Commercial Firm: Non-Demand   | 510                  | \$ 7.50              | \$ 10.00             | \$ 12.50               |
| Commercial Firm: Demand       | 10                   | \$ 292.00            | \$ 390.00            | \$ 485.00              |
| Small Interruptible           | 1                    | \$ 59.75             | \$ 80.00             | \$ 99.50               |
| Medium & Large Interruptible  | 1                    | \$ 1,126.00          | \$ 1,500.00          | \$ 1,880.00            |
| Firm Transportation           | 0                    | \$ -                 | \$ -                 | \$ -                   |
| Interruptible Transportation  | 0                    | \$ -                 | \$ -                 | \$ -                   |
| <b>Total</b>                  | <b>5,787</b>         | <b>\$ 172,000.00</b> | <b>\$ 235,000.00</b> | <b>\$ 298,000.00</b>   |

- Xcel's position is that fee must be based on customer classes shown in table.
- Updated scenario calculates flat fee based on a percent increase in *average* annual charge for each customer class.
- A 3.5% electric increase and 5.0% gas increase = ~\$1.140 million
- Residential customers' electric and gas bills increase \$61.50 annually.

# Potential Inequities in Flat Fee

- Each customer within same customer class pays same amount.
- Small inequities in residential but potential large inequities in commercial and industrial.
- Electric General Service (non-residential) definitions:
  - Small Rate Classes - Less than or equal to 100 kW per day
  - Large Rate Classes - Greater than 100 kW per day

| Example of Discrepancy                       | Average Daily Usage (kWh) | Annual Electric Bill | Annual Franchise Fee (4%)* | Percent of Annual Bill |
|--|---------------------------|----------------------|----------------------------|------------------------|
| <b>Electric Large C&amp;I Customer Class</b> |                           |                      |                            |                        |
| General Service Premise (Actual Data)        | 450 kWh                   | \$16,000             | \$11,880                   | 74.3%                  |
| Peak Control Premise (Actual Data)           | 34,000 kWh                | \$998,000            | \$11,880                   | 1.2%                   |
| Peak Control Premise (Actual Data)           | 5,400 kWh                 | \$230,000            | \$11,880                   | 5.2%                   |
| *\$990 per month times 12 months             |                           |                      |                            |                        |

- Gas Commercial Non-Demand definitions:
  - Small Rate Classes - Less than 6,000 therms per year
  - Large Rate Classes - Greater than 6,000 therms per year

Additional background: Xcel categorizes and bills customers based on multiple criteria, including types of customer and usage

**ELECTRIC CUSTOMER CLASSES**

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**Residential**

**Notes:**

No additional categories

**Commerical**

*Small C&I – Non-Demand*

Max demand < 25 kW

*Small C&I – Demand*

Max demand > 25 kW

*Firm Secondary*

*Firm Primary*

*Interruptible Secondary*

*Interruptible Primary*

*Large C&I*

*Special*

*Firm Secondary*

*Interruptible Secondary*

*Interruptible Primary*

*Interruptible TT*

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**GAS CUSTOMER CLASSES**

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**Residential**

**Notes:**

No additional categories

**Commercial**

*Commercial Firm - Non-Demand*

Small

Less than 6,000 Therms

Large

At least 6,000 Therms

*Commercial Firm - Demand (Peak Daily Demand)*

Small

Less than 500 Therms

Large

At least 500 Therms

*Interruptible (Peak Daily Demand)*

Small

Less than 2,000 Therms

Medium

> 2K and < 50K Therms

Large

More than 50,000 Therms

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## Possible Alternative Solution: Flat Fee on More Specific Definitions of Customer Class - Electric

| <b>ELECTRIC</b>                  | <b>Approx # of Premises</b> | <b>Monthly Franchise Fee</b> |
|----------------------------------|-----------------------------|------------------------------|
| <b>Small C&amp;I: Non-Demand</b> |                             |                              |
| Between 0 - 50 kWh               | ?                           | \$ 2.50                      |
| Between 50 - 100 kWh             | 2                           | \$ 3.50                      |
| Total                            | 485                         |                              |
|                                  |                             |                              |
| <b>Small C&amp;I: Non-Demand</b> |                             |                              |
| Between 0 - 50 kWh               | ?                           | \$ 20.00                     |
| Between 50 - 100 kWh             | 2                           | \$ 30.00                     |
| Total                            | 225                         |                              |
|                                  |                             |                              |
| <b>Large C&amp;I</b>             |                             |                              |
| Between 100 - 500 kWh            | ?                           | \$ 600.00                    |
| Between 501 - 1,000 kWh          | ?                           | \$ 750.00                    |
| Greater than 1,000 kWh           | 2                           | \$ 1,000.00                  |
| Total                            | 55                          |                              |

- Electric General Service (non-residential) definitions:
  - Small Rate Classes - Less than or equal to 100 kW per day
  - Large Rate Classes - Greater than 100 kW per day
- Xcel's position is that fee must be based on customer classes and that any additional usage calculation would not be allowed

## Possible Alternative Solution: Flat Fee on More Specific Definitions of Customer Class - Gas

| <b>GAS</b>                                 |                                 |                                  |
|--|---------------------------------|----------------------------------|
| <b>Gas Commercial Firm:<br/>Non-Demand</b> | <b>Approx # of<br/>Premises</b> | <b>Monthly<br/>Franchise Fee</b> |
| Small Rate Class                           | ?                               | \$ 5.00                          |
| Large Rate Class                           | ?                               | \$ 10.00                         |
| Total                                      | 510                             |                                  |
| <b>Gas Commercial Firm:<br/>Demand</b>     |                                 |                                  |
| Small Rate Class                           | ?                               | \$ 275.00                        |
| Large Rate Class                           | ?                               | \$ 325.00                        |
| Total                                      | 10                              |                                  |

- Gas Commercial Non-Demand definitions:
  - Small Rate Classes - Less than 6,000 therms per year
  - Large Rate Classes - Greater than 6,000 therms per year
- Xcel's position is that fee must be based on customer classes and that any additional usage calculation would not be allowed



## Background on options (previously presented)

### Special Assessments

#### Advantages:

- Common tool to fund and finance infrastructure improvements.
- Relationship between value received / cost of service and amount paid.
- Tax-exempt properties pay for improvements they benefit from.
- Reduces overall property tax rate.
- Can be used to cash flow projects, i.e. reduce size of bond issues.

#### Disadvantages:

- Process is complex, long and expensive
- LMC Guide to Special Assessments is over 100 pages.
- No perfect method for assessing property.
- Special Benefits Test is difficult to prove at times.
- Time consuming to administer.
- Multiple deferral options can make revenue projections difficult.



## How do other cities fund street improvement projects?

- Special Assessments
  - Percent ranges from 0% (Minnetonka) to 100% (Edina)
  - No one method is the same
- Annual Levy for Mill and Overlay
  - Only bond for full street reconstruction projects
- Infrastructure Replacement Reserve Fund (M.S. 471.572)
  - Commonly referred to as a Permanent Improvement Replacement (PIR) fund
  - Provides additional flexibility by pooling funds
  - Can be used to cash flow projects prior to bonding
- Assessment Funds
  - Similar to a PIR Fund
  - Monies used to pay cash for street projects, reducing borrowing amount
  - Future assessments replenish the fund

## Comparable City Information

- Mix of franchise fee revenue uses.
- Majority still assess for improvement projects.
- Elk River eliminated assessments in 2013.
- Created a franchise fee rebate program to reimburse property owners with outstanding assessments.

| City            | Annual Franchise Fee Revenue | Receiving Fund           | Assess for Street Projects |
|-----------------|------------------------------|--------------------------|----------------------------|
| Forest Lake     | \$730,000                    | Capital Projects         | No                         |
| St Louis Park   | \$3,100,000                  | Pavement Management Fund | No                         |
| Owatonna (1)    | Unknown                      | General Fund             | Yes                        |
| Elk River (2)   | \$1,400,000                  | Pavement Management Fund | No                         |
| New Brighton    | \$900,000                    | General Fund             | Yes                        |
| Stillwater      | \$470,000                    | General Fund             | Yes                        |
| South St Paul   | \$1,100,000                  | General Fund             | Yes                        |
| Faribault       | \$761,000                    | GF, DSF, CIP             | Yes                        |
| White Bear Lake | \$309,000                    | General Fund             | Yes                        |
| New Hope        | \$945,000                    | GF & Street Fund         | No                         |

(1) Owatonna Public Utilities (OPU) does not charge the City for electric use. Amount equals approximately 4% of OPU electric revenues.

(2) 2013 rebate program for outstanding special assessments.

## Comparable Cities

- 9 of 13 comparable cities have franchise cities.
- 6 of 13 have franchise fee and assessments.
- All cities either collect franchise fees or assessments.

| City  | Annual Franchise Fee Revenue | Receiving Fund           | Assess for Street Projects |
|---|------------------------------|--------------------------|----------------------------|
| West St. Paul   | \$1,200,000                  | Multiple                 | Yes                        |
| South St Paul   | \$1,100,000                  | General Fund             | Yes                        |
| New Brighton  | \$900,000                    | General Fund             | Yes                        |
| Faribault   | \$761,000                    | GF, DSF, CIP             | Yes                        |
| Stillwater  | \$470,000                    | General Fund             | Yes                        |
| White Bear Lake   | \$309,000                    | General Fund             | Yes                        |
|   |                              | Pavement Management Fund |                            |
| St Louis Park   | \$3,100,000                  |                          | No                         |
|   |                              | Pavement Management Fund |                            |
| Elk River   | \$1,400,000                  |                          | No                         |
| New Hope  | \$945,000                    | GF & Street Fund         | No                         |
| Forest Lake   | \$730,000                    | Capital Projects         | No                         |
| Hastings  | No                           | N/A                      | Yes                        |
| Columbia Heights  | No                           | N/A                      | Yes                        |
| Crystal   | No                           | No                       | Yes                        |
| Owatonna (1)  | Unknown                      | General Fund             | Yes                        |
| (1) Owatonna Public Utilities (OPU) does not charge the City for electric use. Amount equals approximately 4% of OPU electric revenues. |                              |                          |                            |

## Current Trend: Franchise Fees

*Under Minnesota Statute (216B.36), cities can impose a fee on utility companies that use the public rights-of-way to deliver service.*

### Advantages:

- Franchise fees are paid by all properties within the City, including tax-exempt properties.
- Diversifies the City's revenue sources, potentially reducing reliance on property taxes, local government aid and assessments.
- Provides a reliable source of revenue.
- Easy for the City to administer and no administrative costs are charged by the utility companies.

### Disadvantages:

- A flat-rate franchise fee is the same for all residential homes, regardless of the value of their property or utility usage.
- Depending on various circumstances (type of business, utility usage, amount of fee, etc.), franchise fees can be a financial hardship on commercial businesses.
- Like property taxes, franchise fees may make a city less desirable than surrounding communities that do not impose franchise fees.

## Recommendations

- Use General Obligation Improvement Bonds for New Constructions if Authorized by Council Upon Request by Developer
- Use G.O. Street Reconstruction Plan Bonds for Reconstructions and Mill & Overlay  
- Property tax and franchise fees
- Use Tax Abatement Bonds or Cash for Sidewalks, Trails, Others  
- Property Tax and/or franchise fees

| Authorized Uses  | G.O. Improvement Bonds | G.O. Street Reconstruction Plan Bonds | G.O. Abatement Bonds |
|--|------------------------|---------------------------------------|----------------------|
| Repair & Replace Utilities*  |                        |                                       |                      |
| Water Lines  | ●                      | ●                                     | ●                    |
| Sanitary Sewer Lines   | ●                      | ●                                     | ●                    |
| Storm and Gutters  | ●                      | ●                                     | ●                    |
| Repair & Replace Streets   |                        |                                       |                      |
| Reconstruct and Overlays   | ●                      | ●                                     | ●                    |
| Adding Turn Lanes  | ●                      | ●                                     | ●                    |
| Widening Streets   | ●                      |                                       | ●                    |
| Installing New Streets   | ●                      |                                       | ●                    |
| Installing New Curbs and Gutters   | ●                      |                                       | ●                    |
| Improving Sidewalks  | ●                      |                                       | ●                    |
| <i>Exception: Public Safety Function</i>                                 |                        | ●                                     |                      |
| <b>Payment &amp; Process</b>   |                        |                                       |                      |
| Payment Source   | Min 20% Assess         | Any                                   | Any                  |
| Council Approval - Ordering Imp.   | 5/7                    | N/A                                   | N/A                  |
| Council Approval - Bonds   | Majority               | Two-Thirds                            | Majority             |
| Subject to Reverse Referendum  | No                     | Yes                                   | No                   |
| Number of Public Hearings  | 2                      | 1                                     | 1                    |
| Subject to Debt Limit  | No                     | Yes                                   | No                   |
| Timing of Process  | Min 6 months           | Approx 3 mo                           | Approx 3 mo          |
| Cost of Process  | 1% of constr.          | None                                  | \$10K                |
| *Cities can repair and replace utilities under the Street Reconstruction |                        |                                       |                      |
| Plan authority if it is in conjunction with a street project.            |                        |                                       |                      |



# Franchise Fee Implementation Options

## Four Implementation Options

1. Flat fee per utility account
  - *Example: \$4 per month*
2. Percentage of consumption used by each utility account
  - *Example: \$0.0050 per kWh for electric and \$0.040 per therm for gas)*
3. Percent of Revenue
  - *Example: 3.0% of monthly bill*
4. Hybrid of flat fee and percent of usage or revenue
  - *Example: Flat fee for residential and percentage of usage or revenue for commercial and industrial)*

## Implementation Considerations

- *Xcel Energy's policy is to only implement a flat fee structure.*
- Flat rate structure provides stable revenue stream, rather than one based on consumption or revenue.
- Percentage fee structure provides a more equitable fee across all users as it ensures the largest users pay a proportionally higher fee.
- Under a flat rate structure, setting an increasing flat fee for the various customer classes would be a way to mitigate the inequities.
- Financial impact on companies and institutions within the City.



## Special Assessment Background and Considerations

- Approximately \$2.6 million principal outstanding (includes \$1.3 million for 2020 projects)
- Approximately 580 properties with assessments outstanding (includes 2020 projects)
- Average historical assessment revenue is approximately \$500,000
- Due to larger projects and inflation included in 2020-2024 CIP, future assessment revenue is expected to be approximately \$970,000 annually by 2025
- There is no legal authority to forgive outstanding assessments
- Potential Franchise Fee Rebate Program:
  - Property owners with outstanding assessments are rebated franchise fees (annually)
  - Estimated cost is \$50,000 annually beginning in 2022 and decreasing \$5,000 each year





# Franchise Fee Revenue Requirements

- Approximately \$1.2 million needed annually to be budget neutral
  - Minimum staff recommended revenue to be generated to pursue this fee
  - 100% of future annual special assessment revenue
  - Franchise fee rebate program for existing property owners paying assessments
  - Other lost revenue

# Options & Policy Direction

## Option 1: Replace special assessments with franchise fees

- Using flat fee as presented (modeled after 3.5% electric and 5% gas percentage)

## Option 2: Replace special assessments with franchise fees plus added fees for climate goals

- Option 2a. Increase in franchise fee to generate \$100,000 extra.
  - Using flat fee as presented (modeled after 4.0% electric and 5% gas percentage)
  - Funds go to Climate Action Plan implementation or related Carbon Reduction Strategies
- Option 2b. Increase franchise fee to generate some other increment besides \$100,000
  - Funds go to Climate Action Plan implementation or related Carbon Reduction Strategies

## Option 3: Replace special assessments with franchise fees plus added fees for increasing streets and pedestrian trail improvements

- Option 2a. Increase in franchise fee to generate \$100,000 extra.
  - Using flat fee as presented (modeled after 4.0% electric and 5% gas percentage)
  - Funds go to toward expanding street reconstructions, pothole filling, sealcoating, trails and sidewalks, etc.
- Option 2b. Increase franchise fee to generate some other increment besides \$100,000
  - Funds go to toward expanding street reconstructions, pothole filling, sealcoating, trails and sidewalks, etc.

## Option 4: Do not pursue franchise fees and maintain assessment practice



# Assessments vs Franchise Fee: Impact on Residential Users

- Franchise fee approximately 10% of annual assessment cost, but ongoing.

## OPTION 1

- Annual Average Franchise Fee Residential

Gas      \$27.00

Electric   \$34.50

Total     \$61.50

- Average Residential Special Assessment

\$6,800 (can be paid in entirety)

\$680 per year (10-years repayment option)

## OPTION 2 OR 3 WITH ADDITIONAL \$100,000

- Annual Average Franchise Fee Residential

Gas      \$27.00

Electric   \$39.00

Total     \$66.00

- Average Residential Special Assessment

\$6,800 (can be paid in entirety)

\$680 per year (10-years repayment option)



# Assessments vs Franchise Fee: Impact on “most typical” commercial

- Franchise fee approximately 10% of annual assessment cost, but ongoing.

## **OPTION 1**

- Annual Average Franchise Fee Residential

Gas      \$150.00

Electric    \$ 42.00

Total     \$192.00

- Average Residential Special Assessment  
\$6,800 (can be paid in entirety)  
\$680 per year (10-years repayment option)

## **OPTION 2 OR 3 WITH ADDITIONAL \$100,000**

- Annual Average Franchise Fee Residential

Gas      \$150.00

Electric    \$ 48.00

Total     \$198.00

- Average Residential Special Assessment  
\$6,800 (can be paid in entirety)  
\$680 per year (10-years repayment option)



# Tentative Timelines

|  |   |
|--|---|
| October 13 <sup>th</sup>                         | Council Worksession                           |
| October 20 <sup>th</sup>                         | Review Ordinance<br>Call for Public Hearing   |
| October 21 <sup>st</sup> – Nov. 17 <sup>th</sup> | Public Information on Ordinance Consideration |
| November 10 <sup>th</sup>                        | Public Hearing<br>First Reading Ordinance     |
| November 17 <sup>th</sup>                        | Second Reading of Ordinance                   |
| November 18 <sup>th</sup>                        | Notice to Xcel (90-day implementation)        |
| <b>2021</b><br>March                             | Revenue Commencement                          |



# Councilor Questions & Discussion

A. Are you supportive to proceed with timeline including first ordinance consideration next Tuesday?

B. Thoughts on interest to pursue the alternative option related to proposing the modified flat fee to include fixed usage amounts for commercial/industrial?

C. Which of the options are of interest to you based on this update?

Option 1

Option 2

Option 3

Option 4