



City Council Agenda Item Report

Date: Tuesday, June 16, 2020

Agenda Item No. 2020-361- #K.2

Contact: Micah Grau

Subject: Staff report on the franchise agreement with Pedernales Electric Cooperative (PEC) (Deputy City Manager Micah Grau)

1. Executive Summary

Staff will brief the City Council on the City's franchise agreement with Pedernales Electric Cooperative.

2. Background/History

The City's franchise agreement with Pedernales Electric Cooperative expires on December 31, 2020. The agreement was originally entered into in 1970. Under the current agreement, the City collects a franchise fee of 2% on gross revenue received from sales of electric power by PEC within the corporate limits of Buda.

Franchise fees are one of the main revenue generators for the City after sales and property tax. The City also collects franchise fees for gas and telecommunications. The fee is a payment for operating within a city and for using the City's right-of-way to access service lines and to provide service. It is intended to reimburse the public for the use of public land (right-of-way) where assets are often located. The value of the land in which franchise operates has increased since the previous agreement was adopted in 1970 as have the City's costs in managing utilities located in city right-of-way.

3. Staff's review and analysis

City staff is seeking input from the City Council on negotiating the new franchise fee rate. The rate ranges from 2% up to 6.5% in most other cities served by PEC. The franchise fee payment is on gross revenues. However, the fee is considered and factored into the rates charged by the electric provider to the customer. The fee would apply to both commercial and residential customers of PEC.

The City of Kyle's agreement dates to 2017. Kyle charges PEC a franchise fee of 4.5%. San Marcos's agreement dates to 2012. The initial fee started at 6.5% and then decreased to 4.5% after. Leander charges a fee of 4%. The average fee for other PEC cities is in the 3-5% range.

Staff is seeking direction on which rate is best for Buda. This number will also be factored into the Fiscal Year 2021 Budget. City Council may recommend a graduated rate that increases over the term of the franchise agreement.

4. Financial Impact

Under the current agreement with PEC, the City collects a 2% franchise fee which brought in \$463,471 in General Fund revenue in Fiscal Year 2020 off of approximately \$23 million in gross sales to consumers in Buda. The City could generate additional general fund revenue in the amounts shown below if the City were to increase the franchise fee. A full year's worth of revenue with the different options is shown based on the FY 2020 collections. However if the City were to increase the franchise fee through a new agreement, only three out of four quarters would be collected for Fiscal Year 2021 as the new agreement would not take effect until January 1, 2021. Each half of a percentage point of a rate generates \$115,867.75 in franchise fee.

Current 2%: \$463,471

3%: \$695,207

4%: \$926,942

4.5%: \$1,042,810

5%: \$1,158,678

6%: \$1,390,413

5. Summary/Conclusion

Staff is seeking input from the City Council on the franchise fee rate to use for negotiating a new franchise agreement with PEC. The City's agreement expires on December 31, 2020. The rate recommended by Council will also be used tentatively in the Fiscal Year 2021 Budget Proposal. Staff anticipates bringing the franchise agreement to City Council for consideration in late summer or early fall.

6. Pros and Cons

Pros:

1. Increasing the franchise fee rate provides greater diversity in revenue sources and relieves pressure from other sources such as property taxes and sales tax.

Cons:

1. A franchise fee is built into the rate model paid by customers so that the fee is ultimately paid by the consumer as part of their cost for service.

7. Alternatives

The City must negotiate a new franchise fee with PEC so that electric service is provided to Buda businesses and homes. The franchise fee is negotiable.

8. Recommendation

Staff seeks City Council's input and direction on the franchise fee proposal. Staff would recommend a minimum rate of 4.5% inline with other Hays County communities.