


CITY COMMISSION POLICY

GRAND RAPIDS  MICHIGAN	NUMBER: 700- 10	HISTORY
	DATE: April 30, 2013	DATE
	FILE NUMBER: 82367	
	DEPARTMENT: Fiscal Services	

SUBJECT: FULL COST RECOVERY

PURPOSE: Establish a policy regarding the full cost recovery of all user fees

POLICY: USER FEE POLICY

Policy Statement

The City of Grand Rapids shall collect user fees to fully recover the cost of services where it is determined that a service, product or use of the City resources provides a direct benefit to identifiable individuals and groups of individuals, groups, or businesses beyond those services that accrue to the general public.

User fees shall recover the full cost (100%) of providing the applicable service except where the City has approved a subsidy or an exemption for full cost recovery, such as where a service is priced based on competition in the open market or where the fees are legislated by the state or federal government. In any case, the amount of the fee may not exceed the full cost of providing the applicable service.

Summary Background

The Government Finance Officers Association (GFOA) recommends establishing a user fee policy that includes a methodology for calculating the full cost of providing a service that will provide the basis for setting user fees. The GFOA promotes several best practices with regard to developing and implementing a user fee policy. They include:

- Develop and maintain a comprehensive list of services provided and user fee schedules
- Establish a “standard” methodology for full cost calculations for all service provisions to ensure transparency and accountability across departments
- Promote full cost recovery by basing user fees on full costs
- Review the cost recovery considerations and determine optimal cost recovery goals for each service provision for which the City is unable to charge the full service provision cost to users
- Identify the governing body that may determine if a service shall receive less than 100% cost recovery
- Provide criteria for those services which shall receive subsidies and/or for those services to be eliminated
- Establish a schedule for fee review and cost calculation updates

Definitions

User Fees - The City of Grand Rapids collects three kinds of user fees:

- 1) Charges for Services where the exchange of money for services rendered occurs
- 2) Licenses and Permits where individuals purchase the right to do something such as operate a business or obtain a passport
- 3) Fines and Forfeitures where an individual has not paid for a service or did not follow the City's rules and regulations

Cost Recovery - Cost recovery is when the City captures all or some portion of the total costs required to deliver a specific service provision.

Direct Costs - Costs incurred that directly support the service provision or the final cost objective and are 100% assignable to the service provision. For the City of Grand Rapids fee costing methodology, this includes ONLY fully loaded personnel costs for all personnel (full-time, seasonal, temporary, etc.) supporting a particular service, both direct service and administrative support.

Indirect Costs - Costs that consist of departmental, non-personnel costs used to deliver multiple services or cost objectives and are not readily assignable to one particular service provision but can be allocated proportionally (by the distribution of direct costs or some other consistent method) to multiple service provisions. Any departmental costs that are solely related to the service provision (such as vehicles used by inspectors, but not support staff), are to be assigned solely to that service.

Overhead Costs - Costs provided by central service departments that are shared across multiple departments through the A-87 cost allocation plan and are of a general nature that do not relate solely to any major function.

Methodology Overview

The City's objective is to realize full cost recovery. To accomplish this goal, the City of Grand Rapids must reevaluate its current fees and services provided, assess how the fees are calculated, recalculate the total costs to provide the service provision, and identify the value of the service provision relative to the benefit it provides. The City also must implement a standard approach to fee calculation across the many departments. By creating a consistent and standard fee methodology and policy, the City will be able to establish financial transparency and improve its financial accountability and sustainability.

Full costs shall be calculated to determine the appropriate charge for a service or a program. The cost analysis and calculation shall occur for all services and programs independent of whether the objective is to fully or partially recover the cost of providing the service. If the City Commission chooses to subsidize a particular service or program, at least the full cost analysis will provide complete transparency as to the level of subsidy applied to deliver the service or program. Determining full costs can be a very complex process and the City of Grand Rapids needs to put into balance the complexity of accuracy, the ease of use, the ease of maintenance, and need for simplicity. In other words, the effort made in calculating the full costs should be commensurate with the scale of the service or program. Time tracking shall be performed as follows:

- 1) Cross-Departmental Service Provisions – by tracking actual time and expenses (direct and indirect) to a particular service provision via the “Project” functionality in the Microsoft Dynamics GP financial system. Overhead costs shall be allocated by the percentage of direct costs required to deliver a particular service provision.
- 2) Single Department Service Provisions – by using time estimates (updated on an annual basis) and fully loaded personnel cost rates to assign direct costs to a particular service provision. Cost calculations can be performed in Excel to justify service provision costs. Indirect and overhead costs shall be allocated by the percentage of direct costs required to deliver a particular service provision plus any significant costs incurred solely for that service.

Each department shall use all direct costs, all indirect costs, and all overhead costs to determine the total cost for each service provision.

Full Cost Recovery

This policy states that all user fees including permits and licenses and fines and forfeitures should be set at a rate to recover the full cost from those individuals, groups or businesses that receive a direct benefit from the service or where the service is performed at the request of or for the convenience of the recipient.

Full cost recovery establishes a basis on which the City of Grand Rapids may allocate limited resources, reduce the reliance on subsidies, create fair and equitable debates with regard to

service provisions, and improve resource allocation by having individuals, groups, and businesses that benefit from the service pay for the service.

Departments shall accurately calculate the full cost of providing a service notwithstanding the ability to recover 100% of the costs from user fees.

Understanding this relationship between the type of service and the benefits received will guide the City of Grand Rapids in its decision-making regarding the charging of user fees. City services may be categorized into the following major groups:

- **Private Service:** These service provisions benefit individuals, groups or businesses and therefore only specific users opt to take advantage of this service.
- **Private and Public Service:** These service provisions benefit the general public as well as specific individuals, groups or businesses.
- **Public Service:** These service provisions benefit the general public and by nature of the service, it is impossible to exclude any individual from taking advantage of the benefits provided by the service or program.

The major concept supporting this User Fee Policy is that those who receive direct benefits should pay for the service provision. As a result, cost recovery strategies should always take into account the relationship between the service and the benefit to the individual, group, or business to determine if the benefit is predominately private or public. Depending on the type of benefit, the degree of cost recovery may not always be 100%, and further, the pricing may not be based on the full cost to provide the service. On those occasions where only partial recovery is a possibility, justification for recovering less than the full cost must be clearly stated. Promoting this strategy will improve the City's ability to demonstrate transparency and accountability in managing user fees and fee policy decision-making processes.

Considerations for Full Cost Recovery

Once the City has a complete service provision list and has calculated the total costs to deliver these services, it may evaluate what rates of recovery each service should achieve if it believes full cost recovery is not an option. Several considerations may be applied to a service provision to determine its level of cost recovery.

Restrictions by an External Agency. The State or another government agency may set a maximum amount or limit the ability to charge a user fee. The collection of fees in excess of the allowable maximums would not comply with regulatory requirements and/or legislative/governmental restrictions. Examples may include charging for time spent copying and retrieving public documents such as for FOIA requests.

Encouragement or Discouragement of Desired Behaviors. Maintaining fees at certain levels may sometimes encourage improved compliance or discourage "bad" behavior from an individual, business or the community at large. Examples may include keeping the rental certification rates low so that lower-income individuals may find affordable housing or imposing late fee fines.

Effect on Demand for a Service Provision. Increasing the user fee for a particular service may reduce the demand for that service. For example, if the golf greens fees are too high, the customers may seek alternate golfing arrangements.

Considerations for Full Cost Recovery - continued

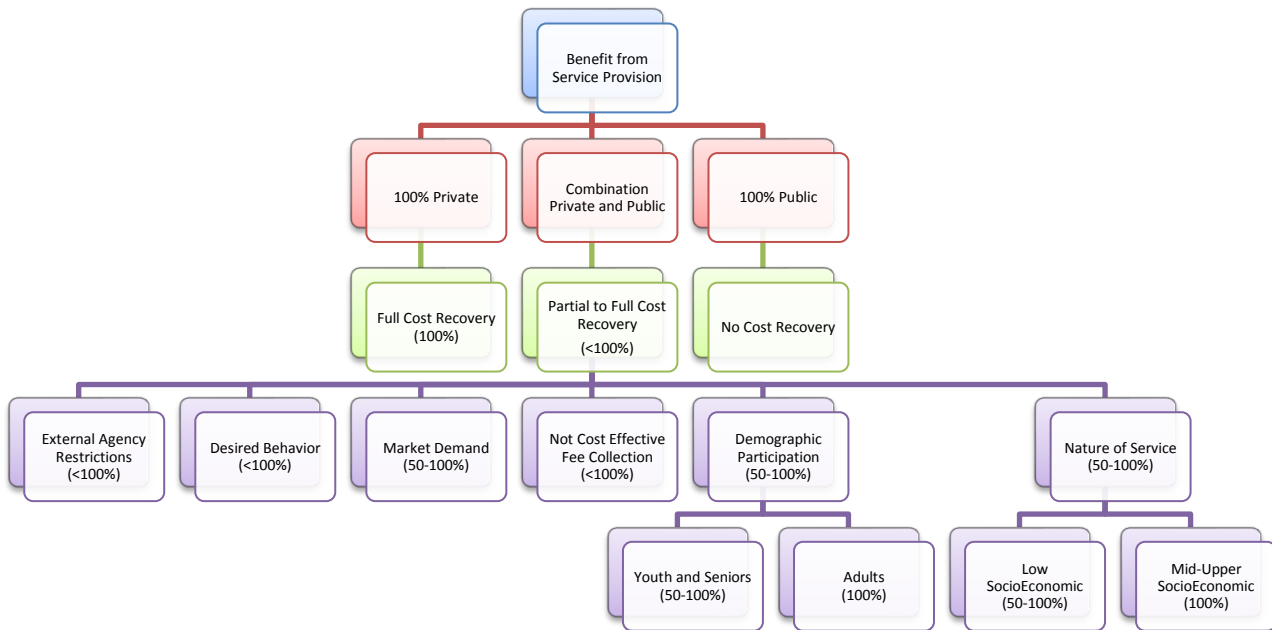
Collection of fees is not cost effective. Collecting full costs for certain services may not be cost effective. For example, collecting an entrance fee to a park could cost more by having to maintain an admissions staff.

Participation by Certain Demographic Segments May be Too Costly. The City may choose to fully subsidize or set fees below full cost recovery so that all members of the community may utilize the service.

Nature of the Service. The service may target youth and/or adult recreation. Depending on the user of the service, the City may choose to increase or decrease the user fees.

After considering these variables, the City should determine to what degree a service should recover its costs, keeping in mind that the overall policy is to achieve 100% cost recovery. In any event, all departments should calculate the full cost of providing their service(s). Justifications for reduced charges (partial cost recovery) must be clearly defined so that the degree of subsidy is transparent to those providing and monitoring the service.

Figure 1: Decision Matrix for City Fee Policy



Note: The recovery rate levels may vary based on the City of Grand Rapids overall policies. 50% is used for illustrative purposes to indicate a cost recovery level less than 100%, yet high enough to justify providing the service.

Timeline for Fee and Cost Review

On an annual basis, as part of the budget review process, the City of Grand Rapids may adjust the fees based on economic factors such as the Consumer Price Index (CPI) or other agreed upon annually adjusted inflators and revised budget allocations. Fees set by the federal or state law or other regulatory body would be exempt from such an adjustment. The inflation factor is only a proxy, or estimate, of cost increases. This does not replace the need for a periodic actual cost analysis (i.e. full review) on a set schedule.

Although no measure is perfect, the most widely applied is the Consumer Price Index (CPI). Given its pervasive use in setting cost-of-living adjustments (COLAs), it can be the appropriate metric when calculating the rate of consumer inflation at the national level. (Source: GFOA)

Without the annual review and required adjustments, the fees may no longer fully recover the costs of delivering the service provision. Consequently, the City will have to find other sources of funding to cover the gap created from insufficient fee revenue. As long as the City policy is to achieve 100% cost recovery, the City must review the user fees on an annual basis.

The City of Grand Rapids will conduct a comprehensive fee review of every fee or family of fees every three years. It is intended that one-third of the departments will undergo in-depth cost analysis of their user fee structure each year, with a review cycle for each department every three years. For the two years between the full review cycle, the departments will adjust the fees based upon the CPI. Any major changes must be approved by the City Commission prior to the adoption of the annual budget for the following fiscal year. When conducting comprehensive fee reviews, the City should answer the following questions:

- Are total service costs covered by the received revenues and if not what is the recovery rate?
- Do the fees recover the total costs and/or generate revenue that may supplement other services?
- What are the current direct, indirect, and overhead costs?
- For those services the City decides only demand partial cost recovery based on one or more cost recovery considerations highlighted earlier in the document, what are the fees charged by neighboring municipalities for similar services? What are the market rates?
- There are services that are not and cannot be delivered on a full cost recovery basis. These services should be reviewed to determine if the services are available from the private sector or from the not-for-profit community. Services available from alternative sources shall be considered for elimination.
- What is the demand level for a specific service and how has it increased or decreased over the prior three to five-year period?

If a completely new fee is established, the City Commission should approve the revised fee before it can be implemented. All new fee proposals shall contain the purpose of the new fee, the justification for the implementation or revision, the fee amount and estimated annual revenue, the annual total service provision cost, the cost recovery rate, the nature and extent of the benefit to the customers, and other relevant information used to determine the revised fee schedule.

Public Notice of User Fee Schedules

The City's Fiscal Services Department shall maintain a complete listing of the authorized processes for fee initiation and modification, as well as public notification requirements. This listing shall include the following information: fee name, accounting code to which fee revenues are credited, description of the service or product provided, authorization for the fee, which entity approves the fee, method of calculating the fee, what share of costs are recovered by virtue of charging the fee, the unit of measure against which the fee is calculated, and the estimated upcoming year revenue for the fee.

Unless otherwise authorized by City Commission, all fee schedules and revised fee proposals shall be made public prior to their submission for approval to the City Commission. The City Commission may automatically approve the annual inflationary adjustments, but all other fees shall be made public by holding a public hearing, to be announced in a paper of general circulation in Grand Rapids, to be held at the City Commission meeting prior to the meeting at which the City Commission will be asked to consider the changes. At the public hearing, interested parties may express any concerns they may have with the proposed fee adjustments.

Conclusion

The purpose of this User Fee Policy is to establish a standard approach to cost recovery calculations and user fee setting for all departments across the City of Grand Rapids. Specifically, the Policy promotes best practices for full cost recovery of user fees and establishes a timeline for updating user fees, so that the City may ensure the perpetuation of full cost recovery year after year.