



December 6, 2023

Results of the FY24-25 Cost Recovery Analysis

The San Diego County Air Pollution Control District (SDAPCD or District) retained the Matrix Consulting Group to conduct an update to its Cost Recovery Study. The following memo provides a background of the project scope, the legal framework within which the cost recovery study was conducted, the methodology used to conduct the study, modifications to the current cost recovery model, the overall results, and the recommended cost recovery scenario.

Project Background and History

The California Health and Safety Code Sections 41512 and 42311 allow the District to recover the full costs associated with the renewal, evaluation, and issuance of permits. These sections also provide limits on fee increases for permit to operate and authority to construct permits, restricting aggregate revenue increases to 15% annually. Based upon this legal authority, the District has a goal to review its fees every year to ensure that all fee-related costs are captured and maximum cost recovery is achieved.

In 2020, the State Auditor issued a report regarding SDAPCD, which identified that fee-related expenses were not being fully recovered. As a result of these findings, the SDAPCD conducted its first external fee evaluation in 2021, with study results presented and adopted by the SDAPCD Governing Board in May 2021¹. Before implementing fee increases in 2021, the District had not raised fees in three years.

At the end of 2021, the Matrix Consulting Group worked with the District to conduct an update to the study conducted earlier in 2021. This update incorporated staffing and budgetary adjustments as well as several fee program modifications. The results of this analysis were presented and adopted by the Board for implementation on July 1, 2022. In September 2022, the Matrix Consulting Group began working with the District to conduct the next update to the Cost Recovery Analysis for implementation on July 1, 2023.

¹ A link to the 2021 Matrix Consulting Group report can be found at: [Cost Recovery Report](#)

As part of the continuing effort to ensure that fees cover the costs associated with their activities, the District is now updating its fees for implementation on July 1, 2024. The goal of this study was to update the analysis from last year based on new inputs associated with staffing, costs, workload, and any changes in fee structures.

2 Legal Framework

The California Health and Safety Code and Proposition 26 are the two primary legal frameworks governing the fees and revenue requirements for Air Pollution Control Districts. Proposition 26 considers all charges imposed by a local government as a tax, except for the following seven exceptions:

1. **Fees and Charges for Specific Benefit Conferred or Privilege Granted:** This is in relation to a payor receiving a service that is only provided to that payor specifically, and the costs for this must not exceed the reasonable costs of providing that service.
2. **Fees and Charges for Specific Government Service or Product Provided:** This is similar to the first exception and is directly in relation to a service or tangible product received, and it must not exceed the reasonable cost of that service or product. This is the exception that is used for “user fees”.
3. **Regulatory Fees and Charges:** This is in relation to issuing licenses and permits, performing investigations, inspections, audits, and administrative enforcement of regulated activities. These charges must be based on reasonable regulatory costs.
4. **Use of Government Property:** This is in relation to using park or government facilities, so purchase, rental or lease of any government owned property.
5. **Fines and Penalties:** This is in relation to any charges that are imposed as a result of violation of local or state regulations.
6. **Fees and Charges Imposed as Condition of Development:** This is in relation to impact fees and requires a nexus of how the development has a specific correlation to the impact.
7. **Property Related Fees and Charges and Assessments:** This is in relation to utility / service fees that are imposed in relation to the property such as water, sewer, trash, etc.

The Air District’s fees fall under the exception #3 primarily with a handful of fees that are under exception #2. The language of Proposition 26, states that the local government must ensure that the fees imposed for any of these exceptions should be based upon the reasonable costs necessary to cover those activities or provide those services.

Additionally, there should be a reasonable relationship that exists between the cost and the benefit borne by the payors of these fees.

The Cost Recovery Model (provided under separate cover to the District) calculates the full cost of conducting regulatory activity and providing any fees for service. These costs include the direct (hands on staff conducting inspections for compliance and reviewing applications), as well as indirect support associated with those activities (i.e., permit processing, rule development, human resources, finance, IT, etc.). The District also ensures that it follows all state and federal guidelines in relation to conducting any compliance inspections or application reviews to ensure that the fee payor is only paying for their fair share of services received. Unnecessary application reviews and inspections are not imposed upon the facility. Any fines and violations for lack of compliance would be imposed separately outside of the fee process.

This study calculates the full cost (direct and indirect) associated with each fee line item assessed by the District. Therefore, for each individual fixed fee, renewal fee, asbestos, or hearing board item, it is ensured that the total fee proposed or recommended does not exceed the full cost of providing the service.

For example, in Rule 40, for Schedule 1X there is a current fixed application fee of \$636. Through the FY24-25 Cost recovery study, the full cost calculated for this fee is \$900. The District is proposing to increase all fixed application fees by 15%, resulting in the recommended fee being \$731. The proposed fee of \$731 does not exceed the full cost of \$900. Conversely, Schedule 13A shows a fixed application current fee of \$3,569 and full cost of \$3,783. As a 15% fee increase would result in the recommended fee being \$4,104 the District is recommending this fee to be set at full cost (\$3,783) or a 6% increase.

Therefore, as the examples demonstrate, even though the District applies a recommended fee percentage increase across the board to a fee schedule, each individual fee is evaluated to ensure that it does not exceed the maximum justifiable full cost fee calculated through the cost recovery model.

Methodology

The work accomplished by the Matrix Consulting Group, in partnership with District staff, to develop the full cost of fee-based services involved the following steps:

- **Staff Interviews:** The project team met with District staff to discuss and determine fee structure modifications and time estimate assumptions.

- Staff provided insight regarding changes that needed to be made to the current fee structure.
- Staff confirmed previous or provided updated time estimates associated with processing, review, and inspection services. These estimates represent average times and exclude extremely difficult or abnormally simple projects.

All fee schedule modifications and time estimate assumptions were reviewed by the project team for “reasonableness”, as well as with District management.

- **Cost Analysis:** Fiscal Year 2023 / 2024 budget and staffing documents were provided by the District. This information was then entered into the Matrix Consulting Group’s analytical software model where several cost components were calculated for each fee or service. The components then build upon each other to comprise the total cost for providing the service.

The methodology employed by the Matrix Consulting Group is a widely accepted “bottom up” approach to cost analysis. This methodology evaluates each individual fee line item and calculates its full cost (direct and indirect) based upon two components:

1. **Time Estimates:** The time it takes to provide the individual service, regardless of how many are performed annually.
2. **Fully Burdened Hourly Rate:** The hourly rate consists of the salaries, benefits, productive working hours², services and supplies³, program overhead⁴, and districtwide overhead⁵. It reflects the cost to the District of the position providing the service. It does not reflect the take home pay of the position.

The time estimates are multiplied by the fully burdened hourly rate to calculate the full cost for each individual line item on the fee schedule.

For example, for Schedule 1X the full cost for application evaluation is calculated by taking the estimated time associated with each position classification (0.30 hours for the Sr. Engineer and 2.5 hours for the Associate Engineer) and multiplying it by their

² The productive working hours reflect a reduction from 2,080 annual hours to 1,610 hours to account for vacation, holiday, sick leave, breaks, and trainings.

³ This captures the overhead costs associated with operating expenses for a program such as vehicles, fuel, software, etc.

⁴ This reflects support from clerical and supervisory staff to oversee the activities, as well as general support activities related to permits, inspections, and applications.

⁵ This reflects the support provided by the Board, Rule Development, Office of Environmental Justice, Support Services, and Administration.

respective fully burdened hourly rates (\$344.58 and \$318.55) to arrive at the full cost of \$900.

In order to calculate the estimated annual cost associated with these activities the \$900 is multiplied by the number of fixed fee applications processed during the previous fiscal year. This allows the District to represent the annual cost associated with administering the specific services for which fees are assessed and not the cost of the overall program.

Modifications to Current Cost Recovery Model

All cost recovery studies are a snapshot in time. The FY22-23 study focused on FY21-22 adopted budget and staffing, as well as FY20-21 completed workload information. Due to the nature of fee studies, the cost assumptions utilized to develop the fees are typically backward looking and based upon the current adopted budget for future fee increases. The concept being that future costs should generally be reflective of current costs. For the FY24-25 Cost Recovery Model, the project team incorporated the following data and assumptions:

- FY23-24 Adopted Budget For District Programs showing personnel and operating expenditures
- FY23-24 Adopted Staffing Levels showing updated staffing levels and staffing costs
- FY22-23 Completed Workload Information
- July 2023 Adopted Fee Amounts
- Conversion of seven (7) fees from Fixed Fees to Time and Material (T&M) and one (1) T&M fee to Fixed Fee to represent the variation in level of effort more accurately
- Consolidation of Fees – 34C was consolidated into 34H and 34G was consolidated into 34D to better reflect the level of effort and equipment type being reviewed and inspected by Engineering and Compliance staff
- Elimination of outdated fees – 15D, 37C, and 38F
- Updated time assumptions for Source Testing and Permit Evaluation Services

These model inputs ensured that the FY24-25 model was updated consistent with the current cost recovery model methodology. It also ensures that future fee increases are based upon the most recent cost, organizational structure of the District, and fee-related processes.

Cost Recovery Results

When comparing FY 23-24 fee-related expenditures⁶ with fee-related revenue based upon FY22-23 workload, the District is currently providing a fee-related subsidy of approximately \$1.9 million or recovering approximately 84% of annual fee-related costs. The following table outlines the District's existing cost recovery levels by major fee category assessed by the District:

Table 1: FY24 (Existing) Annual Cost Recovery Analysis

Fee Category	Revenue at Current Fee	Total Fee-Related Annual Cost	Difference	Cost Recovery %
Initial Application Fees	\$746,829	\$895,240	(\$148,411)	83%
Renewal Fees	\$5,404,568	\$6,192,617	(\$788,049)	87%
Source Testing Fees	\$927,698	\$1,467,944	(\$540,246)	63%
Asbestos Fees	\$1,292,649	\$1,402,296	(\$109,647)	92%
Hearing Board Fees	\$10,914	\$51,643	(\$40,729)	21%
Time & Material	\$1,466,936	\$1,746,909	(\$279,972)	84%
Processing Fee	\$460,459	\$521,164	(\$60,705)	88%
TOTAL	\$10,310,053	\$12,277,813	(\$1,967,760)	84%

The largest source of the District's current deficit relates to Renewal fees. Renewal Fees represent 40% of the District's current deficit, with the next largest impact associated with Source Testing Fees. Currently, this deficit is primarily being recovered through other funding sources rather than through permit holders.

It is important to stress that the fee categories above represent estimated revenue and costs for a range of services provided under each fee category and are not inclusive of other non-fee related components within a program. The annual cost is only reflective of fee-related support provided for those activities and does not encompass the entire program.

Cost Recovery Recommendation

Last year, the Board adopted a fee increase scenario that was targeted at increasing all fees that are subject to the 15% aggregate fee rule. The California Health and Safety Code Section 41512.7(d)(2) states that the District has the ability to increase individual fees for service for permit to operate and authority to construct permits as long as the total revenue for those fee categories does not exceed more than 15% in a single fiscal year.

⁶ Fee-related expenditures only refers to the annual costs associated with fee-related activities. It does not include other non-fee related components within a program. For example, Compliance has a Mobile Source unit, whose cost is not included in this calculation as that cost is not permit or fee-related.

The District has traditionally followed this Health and Safety Code guideline by applying it to Application Fees, Renewal Fees, Time and Material, and Processing Fee categories as those fees fall under the “permit to operate” and “authority to construct” permit category. For all other fee categories – Source Testing, Asbestos, and Hearing Board the District is not bound to any limits on fee or revenue increases other than the requirement that the fee cannot exceed the cost of providing the service. Therefore, under this recommended fee increase, the District is able to apply different cost increases to the fee categories to allow for greater cost recovery for the District.

The Board adopted proposed percentage increases from last year are recommended to also be applied to this year, with two differences:

1. **Asbestos:** The Board increased Asbestos fees by 25% per year for 2 years, and last year increased them only by 15%. In order to achieve maximum cost recovery for next year, only a 10% increase is needed to achieve maximum full cost recovery. The 10% increase is needed to account for increased personnel costs between FY23 and FY24.
2. **Hearing Board:** Hearing Board fees comprise 0.1% of the revenue for the District and as such only 0.42% of its costs. Increasing these fees may result in the Hearing Board fees becoming cost prohibitive, without having a significant revenue impact upon the District. Therefore, it is being recommended that these fees see a 0% increase once again for FY24-25.

The following table summarizes by major fee category, the current cost recovery percentage (FY23-24), whether it is subject to the Aggregate Fee increase of 15%, the projected fee increase percentage for FY24-25, and the resulting FY24-25 Cost Recovery percentage:

Table 2: Proposed Cost Recovery Analysis by Fee Category for FY24-25

Fee Category	Current Cost Recovery %	Subject to Aggregate Cap of 15%?	FY24-25 Fee Inc. %	FY24-25 Cost Recovery %
Initial Application Fees	83%	Yes	15%	91%
Renewal Fees	87%	Yes	15%	97%
Source Testing Fees	63%	No	15%	73%
Asbestos Fees	92%	No	10%	100%
Hearing Board Fees	21%	No	0%	21%
Time & Material Fees	84%	Yes	15%	96%
Processing Fees	88%	Yes	15%	99%

The District’s current cost recovery for its fees ranges from a low of 21% for Hearing Board to a high of 92% for Asbestos. The highlighted rows in the table above represent those categories that are subject to the 15% revenue limit, meaning the total revenue for

those fees combined cannot exceed 15%. As the table indicates, fee categories that are subject to the cap of 15% revenue increase, the fee increases are all set at 15%. For all other fee categories, other than Asbestos, the fee increase is the same as the last fiscal year and Board adopted increase. The following table shows for each of the major fee categories, the current revenue based on FY23-24 budgeted staffing and expenditure costs and FY22-23 workload, the projected revenue at the proposed FY24-25 fee percentage increase, and the resulting revenue change:

Table 3: Proposed Revenue Increase Impacts

Fee Category	Revenue at Current Fee	Total Projected Revenue	\$ Difference
Initial Application Fees	\$750,138	\$814,289	\$67,460
Renewal Fees	\$5,382,731	\$5,999,753	\$595,185
Source Testing Fees	\$927,698	\$1,065,388	\$137,690
Asbestos Fees	\$1,292,649	\$1,397,425	\$104,776
Hearing Board Fees	\$10,914	\$10,914	\$0
Time & Material Fees	\$1,466,936	\$1,676,123	\$209,187
Processing Fees	\$460,459	\$513,882	\$53,423
TOTAL	\$10,291,525	\$11,477,774	\$1,167,720

The District's total revenue would be projected to be increased by an estimated \$1.2 million from \$10.3 million to \$11.5 million. The largest increase in revenue would be renewal fees estimated at \$593,000, followed by Time & Material fees estimated at \$209,000. The estimated \$1.2 million would represent a 11% increase in revenue for the District and **would result in the District's fee-for-service cost recovery increasing from 84% to 93%.**

When the District first started this study process in 2021, the fee-for-service cost recovery was calculated at approximately 66%. This is the District's fourth year of conducting the study and update, and it will result in getting fee-for-service cost recovery to approximately 93%. The original study had estimated that it would take the District more than 5 years to get to full cost recovery (barring any operational and major cost changes), and as such, the District is on track towards achieving maximum fee-related cost recovery.

As the District gets closer to cost recovery, there will be less of a need for significant annual fee increases. Once fee-related cost recovery is achieved, annual fee increases will only need to match annual cost increases associated with personnel and operating expenditures.

The following table summarizes the advantages and disadvantages of the proposed fee increases from the perspective of internal (District) and external (permit and fee holders) stakeholders:

Table 4: Cost Recovery Recommendation – Advantages and Disadvantages

Advantages	Disadvantages
<ul style="list-style-type: none">• Internal: Increased revenue for the District.• External: Lower fee increases for Asbestos and no fee increases for Hearing Board.• External: Continued focus on ensuring that receivers of the service are paying for their fair share of the service.	<ul style="list-style-type: none">• External: Continued fee increase for rate payors.

The proposed fee increases are consistent with previously adopted Board practices, enables the District to continue its movement towards increasing cost recovery, and applies fee increases based upon estimated level of cost recovery.