

## Background for Discussion

### Possible Adjustment of Processing Payment

CalRecycle Monthly Meeting May 17, 2011

#### Issue:

Scrap values rose rapidly since Fall 2010 and have remained high for five consecutive months. The processing payment given to recyclers is a subsidy to ensure those recyclers do not lose money when scrap values are below the actual cost of recycling a material type. The Department has permissive authority to raise or lower the processing payment to recyclers if scrap values change by more than 5% in the prior 12-month period from the scrap value used to calculate the present processing payment. As the scrap values for glass, PET plastic and HDPE plastic have all risen by anywhere from 7% to 29% since the last processing payment calculation, the Department is contemplating a reduction in the processing payment, effective July 1, 2011. Any adjustment must be communicated prior to June 15, 2011.

#### Background:

The "cost of recycling" some commodities exceeds the value of those commodities. For instance, a recycler will incur about \$84/ton in cost to move a ton of glass from consumers to a processor. The market scrap value a processor will pay the recycler for that glass is generally about \$4/ton. Absent some other source of support, the recycler would lose about \$80/ton for recycling glass. This situation -- cost of recycling (COR) exceeding scrap value (SV) -- has existed since the beginning of the Beverage Container Recycling and Litter Reduction Program (Recycling Program) for glass and all plastics. Since its initial enactment, the Recycling Program made accommodation for that discrepancy with a "processing payment" to recyclers.

The Processing Payment is the difference between the COR and the SV, by material type. If COR minus SV is negative, then scrap exceeds cost and the recycler and no processing payment is established. If the COR minus SV is positive, scrap is less than cost and a processing payment is established. Obviously, Processing Payments differ by material type, as demonstrated by the table below.

<b>Processing Payments, effective Jan 1, 2011</b>			
<b>Material Types</b>	<b>Glass</b>	<b>#1 PET</b>	<b>#2 HDPE</b>
Cost of Recycling (surveyed in 2009 and adjusted for inflation)	\$84.49	\$451.88	\$519.44
Scrap Value Per Ton (2010 survey)	\$4.24	\$307.55	\$280.85
Processing Payment Per Ton, as of 1/1/2011	\$80.25	\$134.33	\$238.59

Monies for Processing Payments come from two sources, an amount contributed by beverage manufacturers and the remainder from unredeemed CRV. Beverage manufacturers pay a percentage of the Processing Payments (calculated to a per-container amount), where the percentage is set by a statutory sliding-scale based upon the material's recycling rate. Thus, manufacturers who package in glass and HDPE plastic pay 10% of the Processing Payment for each container they sell and manufacturers who package in PET plastic pay 11%. The amount the manufacturers pay per container is called the Processing Fee.

The COR value is surveyed every other year and adjusted in the interim year for inflation. By statute, COR cannot change during the calendar year and the amount manufacturers pay cannot change, save on January 1 of each year for the annual Processing Fee. Reports about SV are made monthly to CalRecycle with recycler and processor reporting. Because scrap values can be volatile, statute allows CalRecycle to adjust the amount of the Processing Payment if the prior 12-month average SV is different by more than 5% than the SV used for the most recent Processing Payment. If SV falls by more than 5%, CalRecycle has the authority to increase Processing Payment amounts to account for the loss; if the SV rises more than 5%, CalRecycle can reduce the Processing Payment.

Pursuant to 14575(f), CalRecycle can make these adjustments in the Processing Payments only after the 5% SV change has been observed. An adjustment can only be made once every three months. Funds must be available in the Recycling Fund to make the payments, and the adjustment must be "necessary to further the objectives" of the Recycling Program. CalRecycle must give a minimum of 15 days notice if it decides to adjust the Processing Payment.

Since the end of the SV survey period for the January 1, 2011 Processing Fees/Payments (October 2010), CalRecycle has noticed significant and consistent increases in the SV for all materials, but notably for PET. Those increases are noted in the table below:

<b>Change in Scrap Value Per Ton and Possible Adjustments to Processing Payments</b>			
<b>Material Types</b>	<b>Glass</b>	<b>#1 PET</b>	<b>#2 HDPE</b>
Cost of Recycling (surveyed in 2009 and adjusted for inflation)	\$84.49	\$451.88	\$519.44
Scrap Value Per Ton (Basis of Current Processing Payments)	\$4.24	\$307.55	\$280.85
Scrap Value Per Ton (April 10 – March 11)	\$4.68	\$397.09	\$301.96
Percent Change	<b>10.38%</b>	<b>29.11%</b>	<b>7.52%</b>
Current Processing Payment Per Ton (Effective 1/1/11)	\$80.25	\$134.33	\$238.59
Possible Processing Payment Per Ton, if adjusted	\$79.81	\$44.79	\$217.48

The Recycling Program has contemplated lowering Processing Payments in the past, owing to increased SV. At the time, Payments were not reduced because cost of recycling appeared, by anecdote, to be increasing at the same time (notably, transportation costs). Because those increased costs would not be considered until future COR surveys, reductions in the Payment were not made in the interest of "furthering the objectives of the division" (Division 14 of the Public Resources Code, aka "the Recycling Program"). Reductions in Payment in the face of forces that could otherwise counteract each other (higher SV AND higher COR) could actually have been harmful to recycling center operations and not simply ensuring that recyclers Processing Payment support wasn't too high.

**Conclusion:**

CalRecycle raises this issue to seek input about a pending decision, which should be made on before June 15, 2011. Some considerations raised to date include the following:

SV increases have been correlated to increased demand for post-consumer material and to increases in oil prices (feed stock source for plastic resins), as well as other factors. It is not clear hat has driven SV high for materials and whether those economic forces will sustain the current SV.

Fuel costs for transportation are again high, with gasoline at or above \$4.00/gallon. It is not clear how transportation costs may be rising with scrap values. As before, should the Payment be reduced for rising SV at the same time COR is also rising? Would that be in the best interest of "furthering the objectives" of the Recycling Program?

The savings associated with this reduction are roughly \$7.9M. When the actual Processing Fee/Payment for 2012 is announced, it will include all of these high SV months, though only reflect the COR from 2010 (survey is conducted this year and examines the last full year -- last CY). At that point, the savings from the higher SV will be realized. Is saving approximately \$7.9M when those savings will begin on January, "furthering the objectives" of the Recycling Program? Can the Recycling Fund afford to NOT make the reduction and realize the \$7.9M M savings?