



Fresno County Exclusive Service Area Program Recycling Market Analysis

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Summary

The Exclusive Service Area Program (ESAP) haulers have proposed that they be allowed to charge a premium based on dramatic changes in market prices that have occurred over the past year due to bans and restrictions on recyclables being sold to China. This was discussed with ESAP haulers and staff on June 4, 2018 and with the Board of Supervisors (Board) on June 5, 2018. The Board directed staff to research this issue and report back to the Board. Staff asked Abbe & Associates to review data provided by the ESAP haulers and recommend appropriate actions.

Four of the nine ESAP haulers responded to the County's request for information and provided applicable data. Based on information provided by four ESAP haulers, the total potential impact of the decrease in recycling revenues and increase in costs for more processing to prepare materials to meet current market specifications is 1.45% of estimated gross revenues. Accounting for just the unanticipated costs for moving recyclable materials to markets would be 1.0% of gross revenues.

Section 7.2 of the Amended and Successor ESAP Agreements provides a detailed process for haulers to request a rate adjustment due to Unforeseen Circumstances.

The Board could:

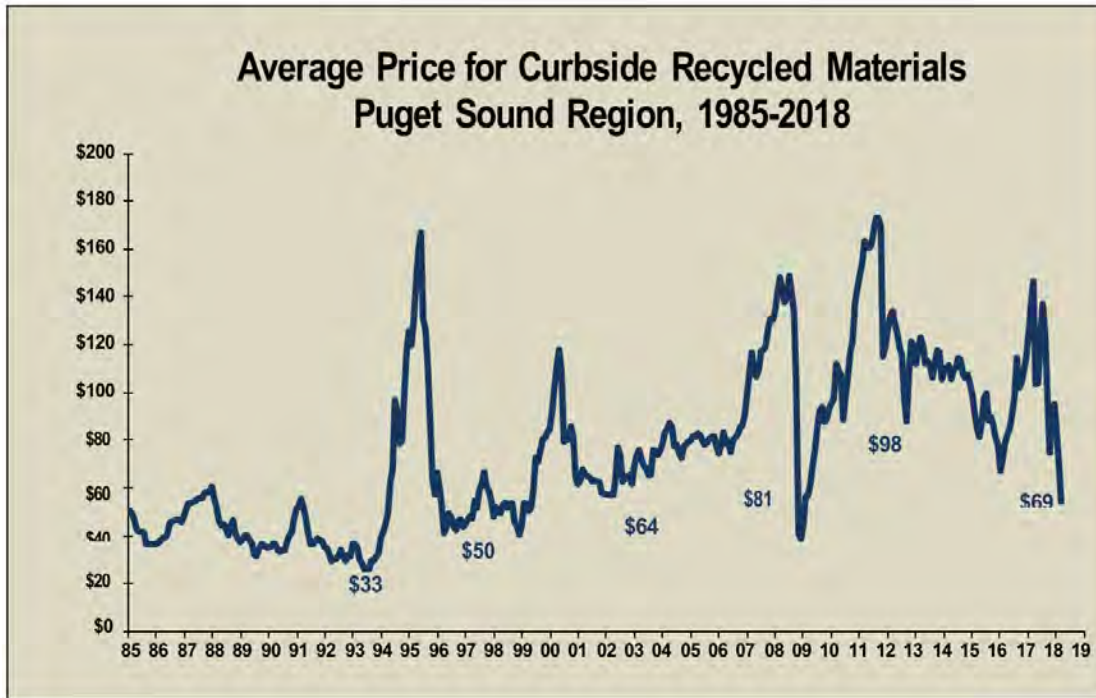
- 1) Direct ESAP haulers and staff to follow the provisions of Section 7.2 to initiate a formal request for a rate adjustment due to Unforeseen Circumstances.
- 2) Direct staff to negotiate a limited amendment to the ESAP Agreements to add only a recycling surcharge and rebate provision (but not consider any other amendments).
- 3) Delay action for either of the foregoing options – allow the recycling commodity loss to be absorbed by the ESAP haulers for a period of one (1) year and direct staff to return to the Board at that time with an update. This option would allow County staff to monitor the recyclable commodity prices over an extended period of time and then potentially consider a rate adjustment, if substantiated at that time.

Analysis

Recycling market prices fluctuate dramatically, as they are the epitome of global commodities. Although data is not readily available for Fresno County, the firm Sound Resource Management in Olympia, WA uniquely maintains great historical data for markets information that can be used as a proxy for understanding the dynamics of recycling markets. Figure 1 shows the changes in market prices since 1985 in the Puget Sound area around Seattle.¹ Between 2007 and 2018, this Figure shows a change from \$81 per ton to \$69 per ton, a decrease of \$12 per ton or 15%.

¹Dr. Jeffrey Morris, *Sound Resource Management, Rhythms & Reasons in Recycling Markets*, presentation on TRUE Zero Waste Markets Webinar, U.S. Green Building Council, May 22, 2018.

Figure 1 Recycled Materials Market Fluctuations



Fresno County staff requested data from the ESAP haulers on market prices for all recyclable materials collected in the Fresno County unincorporated area for all of Calendar Year 2017 and for January through May 2018. The County received submittals of the data requested from four of the ESAP haulers (Allied Waste Services, Mid Valley Disposal, Miramonte Sanitation and Waste Management). Two other ESAP haulers (Tule and Peña's) did respond, but the data they provided was either inapplicable or incomplete. Three ESAP haulers (Granite, IWS, and Western) declined to participate.

The average market price for all residential recyclable materials in Fresno County reported during the first five months of 2017 was \$8.72 per ton (the ESAP haulers received revenues for their recyclable materials). For comparison, the average market price for all residential recyclable materials in Fresno County reported during the first five months of 2018² was negative \$16.69 per ton (the ESAP haulers incur costs to move the recyclable materials to market). The reduction is \$25.42 per ton for residential recyclable materials. For commercial recyclable materials, the average price was \$8.76 per ton in January-May 2017 and in January-May 2018 was negative \$4.20 for a reduction of \$12.96 per ton.

Table 1 Average Revenues/(Costs) Per Ton for Recyclable Materials for ESAP Haulers

	Jan-May 2017	Jan-May 2018
Residential	\$8.72	(\$16.69)
Commercial	\$8.76	(\$4.20)
Average	\$8.74	(\$10.45)

The County has no knowledge as to what portion (if any) of the overall solid waste collection rate was anticipated by the ESAP haulers to be supplemented by recycling revenues. The ESAP agreements do not determine actual costs for the services provided.

²2018 data was only provided through May 2018

Instead, to provide a common basis of comparison, the percent of reported ESAP recycling revenues were calculated compared to total ESAP revenues. Total 2017 ESAP revenues for the four ESAP haulers that provided applicable data were calculated to be \$20.9 million based on the 1% franchise fees ESAP haulers paid to Fresno County in 2017. Total recycling revenues for 2017 from both residential and commercial accounts for those reporting data to the County for this analysis were \$77,836. The percentage of reported recycling revenues to total gross revenues is 0.4%.³

Beyond Fresno County, and in similar contracts to the ESAP Agreements, where revenues from the sale of recyclable materials are not shared with the jurisdiction, haulers do not rely on recycling revenues to cover their processing costs. These revenues are usually considered as providing extra revenue to increase profits. The original and the Amended and Successor ESAP Agreements allow the haulers to retain all revenues from the sale of recyclables. However, haulers have generally not budgeted for it to cost them money to move recyclable materials to markets. Processors have also had to add additional sorting equipment and labor to clean up the materials to meet the new market specifications, incurring additional costs beyond the loss of revenues.

Table 2 lists the total recycling tons collected and revenues received (or costs incurred) by the four ESAP haulers providing applicable data for the first five months of 2017 compared to the first five months of 2018.

Table 2 Tons and Revenues/(Costs) for ESAP Haulers

	Jan-May 2017	Jan-May 2018
Tons	5,809	5,528
Revenues (Costs)	\$51,069	(\$107,113)

The total potential impact of the decrease in recycling revenues and increase in costs incurred for processing and marketing is \$158,182. This is 1.45% of the estimated gross revenues of \$10.9 million for this same five-month period. Accounting for just the unanticipated costs of \$107,113 for moving recyclable materials to markets would be 1.0% of gross revenues.⁴

Based on the foregoing, the Board has several options, including:

- 1) Direct ESAP haulers and staff to follow the provisions of Section 7.2 to initiate a formal request for a rate adjustment due to Unforeseen Circumstances.
- 2) Direct staff to negotiate a limited amendment to the ESAP Agreements to add only a recycling surcharge and rebate provision (but not consider any other amendments).
- 3) Delay action – allow the recycling commodity loss to be absorbed by the ESAP haulers for a period of one (1) year and direct staff to return to the Board at that time with an update. This option would allow County staff to monitor the recyclable commodity prices over an extended period of time and then potentially consider a rate adjustment, if substantiated at that time.

³\$77,836 divided by \$20,914,277 = 0.4%

⁴\$158,182 divided by \$10,893,709 =1.45%
\$107,113 divided by \$10,893,709 =1.0%

1. Unforeseen Circumstances

Article 7 (specifically Sections 7.2 and 7.3) of each ESAP Agreement provides that:

- Should either Party initiate a formal request for a Rate adjustment review, COUNTY shall have the right to review any or all costs associated with CONTRACTOR's services under the Agreement.
- CONTRACTOR must submit, at least six (6) months prior to the proposed effective date of any Rate adjustment, any request for an Unforeseen Circumstance review of Rates, together with sufficient supporting cost and operational data in a form and manner acceptable to the COUNTY Representative... CONTRACTOR [must] also [send] copies of such request to all other exclusive providers of Collection Services operating within the Service Rate Area at issue.
- CONTRACTOR shall bear the burden of justifying to COUNTY by Substantial Evidence any request by CONTRACTOR for consideration of a Rate adjustment.
- Because Rates are intended to be uniform throughout the entire Service Rate Area that includes CONTRACTOR's Exclusive Service Area, the CONTRACTOR is required to provide evidence that supports or justifies application of the requested Rate Adjustment throughout the entire Service Rate Area.

This request would be classified as an "Eligible Item" under Part (b) of Subparagraph 7.2.B.1 of the ESAP Agreement, and the Board may consider this request in accordance with those provisions. The extent to which substantial evidence may provide support for this request is merely one of the factors the Board of Supervisors, in the reasonable exercise of its discretion, may consider relevant to its determination.

This option would not require an amendment to the ESAP Agreements. However, its drawback is that the rate adjustment process is designed for a one-time request and would not provide for any flexibility to address on an ongoing basis the fluctuating impacts of recyclable commodity prices.

2. Recycling Surcharge and Rebate

Alternatively, the County may consider a limited amendment to the ESAP Agreements to include a recycling surcharge and rebate provision that would allow the ESAP haulers to charge their customers to recover the current negative costs (or some portion thereof) associated with moving recyclable materials to markets. This could be done on a biannual basis, after six months of data are provided to the County. The County should not allow haulers to recover any costs of landfilling these materials, as that would cause a disincentive for haulers to continue to recycle those materials.

The recycling surcharge and rebate provision would require that the ESAP haulers eliminate the recycling surcharge once the average quarterly revenues for recyclables return to the levels received in early 2017 prior to the implementation of China's latest restrictions (\$8.74 average revenue per ton). Once revenues exceeded the levels received in early 2017 (\$8.74 average revenue per ton) for two consecutive quarters, ESAP haulers would be required to provide their customers with a recycling rebate.

To protect the ratepayers on the downside and the ESAP haulers on the upside, the recycling surcharge and rebate each could be limited to a percentage range (e.g., plus or minus 3%) of gross revenues.

The recycling surcharge and rebate provision should also require that all ESAP haulers must:

- Provide the requested data, to substantiate the rate increase
- Agree to report all revenues for recyclable materials on a quarterly basis, and
- Provide increased public education/outreach dedicated to the recycling contamination issue (e.g., newsletters, billing inserts, flyers).

This provision would require that the County negotiate a limited amendment to the ESAP Agreements. It would also require on-going reporting of recycling revenues by the ESAP haulers and on-going evaluation of data by County staff.

3. Delay Action

The County could delay action in moving forward with either of the foregoing options. As discussed, recyclable commodity prices are volatile. Alternative markets are available for most commodities that have been rejected by China. Many California processors have modified their operations to sort commodities desired by domestic or other international markets. Many California haulers have provided outreach and education to their customers to sort materials properly to reduce contamination. Few California communities have adjusted their rates in response to market conditions identified by their haulers and processors. While it is possible that recycling revenues will not return to early 2017 levels, the estimated impact of the costs related to moving recyclable materials to markets (1.0-1.45% of gross revenues) is not significant and can be borne through reduced operating profits and belt-tightening.

Five out of the nine ESAP haulers did not provide the County with the requested information (three declined to participate and two provided non-relevant or incomplete data). We assume that the impacts of the recycling costs were not significant enough to warrant their participation or were not relevant to their operations.

Recommendation

We recommend that the County delay action on the ESAP haulers' proposal to allow them to assess a recycling surcharge and direct staff to continue to monitor recyclable commodity prices. Should the ESAP haulers formally request a rate adjustment or propose an amendment in early 2019, County staff could return to the Board with additional information for its consideration.