RE: Processing Payment Emergency Regulations

DATE: December 10, 2019

FROM: Susan Collins, President, Container Recycling Institute (CRI)

TO: Sharon Siozon; OAL Reference Attorney:

Sent by email: sharon.siozon@calrecycle.ca.gov, BevContainerRegs@CalRecycle.ca.gov, staff@oal.ca.gov

CC: DORRegulations@calrecycle.ca.gov, Scott.Smithline@CalRecycle.ca.gov, Adam.Tauber@CalRecycle.ca.gov

Dear Ms. Siozon and OAL Reference Attorney,

The Container Recycling Institute (CRI) supports the 10% reasonable financial return (RFR) as proposed in the Processing Payment Emergency Regulations (CCR Section 2975, Subchap. 12, Chapter 5, Division 2 of Title 14). CalRecycle’s “Finding of Emergency” is correct to choose to stop using Dun & Bradstreet data for return on costs. This decision will create a stable and truly “reasonable” financial return.

At the same time, we must emphasize that the 10% RFR in and of itself only addresses the profit percentage, and doesn’t address the main calculation of payments to redemption centers, which are the processing payments and handling fees. We seek to ensure that the administrative record is complete and correct, and so we are including information here that would otherwise be missing from the records.

Stabilizing the redemption system now is crucial because only 1,209 all redemption centers (RCs) are open for business today: fewer than half of those operating in 2013 (2,578: a 53% loss).

- Compared to 2018, redemption centers are receiving $46 million less per year in aluminum can scrap value: as the graph at right shows, the value of an aluminum bale dropped by $420 between July 2018 and June 2019, spelling plummeting revenue for RCs.

- Scrap revenue shortfalls in glass and PET plastic have created losses for several years in a row: the gap between Cal Recycle’s anticipated scrap revenue and actual scrap revenue has led to a $67.5 million loss in RC revenue over 7 years ($9.6 million per year on average).

- Minimum wage increases are inadequately accounted for in payments to RCs. The handling fees and processing payments are based on 2016 cost surveys, when minimum wage was
$10/hour. It is going up to $12 in 2020, and the annual COLA does not captures the magnitude of this change, as we discuss below.

Here we lay out these issues in more detail:

- **Aluminum revenue no longer the cash cow it once was.** Recycling centers have long relied on aluminum cans to partially “carry” lower-value glass and plastic. But the average price for aluminum cans dropped by $420 per ton, or 29%, since July 2018, as the figure above shows. When this loss is multiplied by the 6.3 billion CRV cans recycled at redemption centers, it equals approximately **$46 million in revenue lost.**

- **Labor costs are inadequately accounted for.** CalRecycle’s cost surveys are conducted every two years, and the values being used now do not include recent minimum wage increases. The processing fee reports are published 2 years after the cost surveys are conducted, so this will be a recurring problem.

The “Finding” states that a minimum wage supplement is unnecessary because a cost of living adjustment (COLA) is applied to the cost of recycling (apart from the RFR). This is partially true, but not entirely. The CPI multiplier used in COLA has hovered around 2-3% per year, or about **10% over 4 years,** whereas in redemption recycling—where labor accounts for roughly 50% of all operating costs—labor costs will have increased by 30% between 2017 and 2021 ($10 to $13/hour), or by **15% of total costs** (30% x 50%). **In other words, minimum wage increases are a large cost increase that is not fully covered by the COLA adjustment.**

- **Race to the bottom:** the formula for calculating the average cost of recycling is **structurally designed** to produce lower average costs as higher-cost redemption sites go out of business. This method virtually guarantees that centers with above-average operating costs will remain in the red, and that closures will continue. In previous letters, we’ve referred to this as a “death spiral.”

- **Scrap revenue calculation methodology puts recyclers at risk of loss.** As CRI has previously reported, the practice of calculating processing payments using outdated scrap values (12-month averages from the previous year—with a minimum three-month lag time) means that in a downward trending market—like the current one—there can be a **significant gap between the averaged values CalRecycle uses to calculate processing payments, and actual scrap values** during the period, as Figure 1 shows. Since 2012, these gaps, or shortfalls, have averaged $39 per ton of PET bottles, and at times have exceeded
$100 per ton. From June 2012 to June 2019, the cumulative shortfalls for glass and PET were $67 million.

- **New transportation costs** are not accounted for at all. Recent bankruptcies of recycling processors—the intermediaries who purchase bottles and cans from redemption centers and sell them to end-users/manufacturers—has led to some processors going out of business. This means that many redemption center operators (or their agents) must now haul their recyclables farther away for processing, leading to higher transportation costs.

In sum, the combination of **inadequately assessing labor costs**, using **average costs for all recycling centers**, and using **backdated scrap values that** fail to account for plummeting actual scrap values has created unprofitable operating conditions for many recyclers. Unless these issues are addressed, closures will continue, and Californians’ access to redemption opportunities will become increasingly limited.

A fixed 10% RFR is reasonable, but only the in context of all costs being covered. A fixed 10% RFR would be a sufficient profit if all costs were offset by revenues (including CalRecycle payments). However, they are not. To date, recyclers have experienced **more than $67 million in cumulative shortfalls for glass and PET recycling in prior years, plus an additional loss of more than $40 million in reduced aluminum revenues in 2019 alone.**

As long as these structural problems remain in place, a 10% RFR will not provide recyclers with a profit; it will only get them slightly closer to breaking even.

**Other reference documents from CRI:**

CRI has communicated to CalRecycle our concerns that inadequate processing payments would lead to redemption center closures since 2016:

1. In April 2016, CRI released an updated report, “Integrity of California’s Beverage Container Deposit System Threatened by Processing Payment Shortfalls.” In it we discuss how falling scrap prices and inadequate processing payments had led to a cumulative operating shortfall of $43 million for glass and PET and the closures of 421 redemption centers in one year. Since that time, cumulative shortfalls have risen to $67.5 million, and more than 800 additional redemption centers have closed.

2. In October of 2017, we wrote in support of emergency regulations to change the reasonable financial return, applauding CalRecycle’s leadership.

![Shortfalls in processing payments for glass and PET, July 2012 - June 2019*](image)
3. On December 10, 2018, CRI wrote CalRecycle in favor of the emergency regulations for 2019. We wrote that the proposed RFRs of 11% and 16% for rural sites were “nowhere near enough to avert the impending financial crisis for redemption centers,” and we recommended doubling them.

4. On August 23, 2019, shortly after rePlanet closed all 284 of their redemption sites in one day, we wrote again, explaining that a 10% RFR would be a good profit if all costs were already covered, but “only 70-80% of RC costs are covered now, [so] a 10% RFR value doesn’t provide enough revenue for centers to cover their costs.” We proposed that CalRecycle design a dynamic process for calculating and adjusting the RFR at regular intervals, based on changes in scrap values, prevailing wages, and other operational costs. *Since August 2019, 17 more RCs have closed, averaging five closures per month.*

Please refer to our four enclosures for further details on the operational costs and revenues for California redemption centers.

If you have questions, I can be reached at scollins@container-recycling.org or 310-559-7451.

Respectfully Yours,

Susan V. Collins
President, Container Recycling Institute

**Enclosures:**
- CRI letter to CalRecycle dated October 13, 2017
- CRI letter to CalRecycle dated December 19, 2018
- CRI letter to CalRecycle dated August 23, 2019