

California Carpet Experience Shows “Visible Fees” May Not Be the Product Stewardship Panacea

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Just before Christmas, the California Department of Resources Recycling and Recovery (CalRecycle) rejected a plan submitted by the industry-sponsored Carpet America Recovery Effort (CARE) to extend the state’s existing California Carpet Stewardship Plan after it expired on December 31, 2016. The plan is intended to assure continued compliance with the state’s used synthetic carpet stewardship statute, generally referred to as AB 2398.¹

Most state product stewardship laws impose on “manufacturers” the responsibility to both manage and pay for end-of-life diversion and recycling programs. But AB 2398 provides that programs will be financed with a “visible fee” imposed on retail customers, leaving “only” program promotion and implementation. Many in business have seen this approach as to manufacturers reasonable and acceptable. The ongoing California experience suggests otherwise.

The rejection triggered a four-month period for a new plan to be developed and approved. At the same time, CalRecycle signaled that it might initiate enforcement action against carpet manufacturers for the failure of its existing plan to meet the requirements of the currently-approved plan. More on that below, at the end of this article. First, however, some background and a review of what the carpet industry faces today.

AB 2398 and its Requirements

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AB 2398 was enacted in 2010. It aimed to “increase the amount of postconsumer carpet that is diverted from landfills and recycled into secondary products” by “working *to the extent feasible* with the carpet industry and related reclamation entities.”²

AB 2398 required that carpet manufacturers establish stewardship programs that would increase recycling, recyclability, and diversion of synthetic carpet (nylon, PET, etc.) by “incentivizing the market growth of secondary products made from postconsumer carpet,”³ complying “with [California’s] solid waste management hierarchy,”⁴ and providing education and outreach to “consumers, commercial building owners, carpet installation contractors, and retailers,” among other things⁵.

Manufacturers’ plans were to “demonstrate to the department that [they had] achieved *continuous meaningful improvement in the rates of recycling and diversion of postconsumer carpet* subject to its stewardship plan and in meeting the other goals included in the organization plan”⁶ This was to be done “*to the extent feasible* based on available technology and information” while at the same time “not [creating] an unfair advantage in the marketplace.”⁷

Unlike most other state product stewardship laws, however, the cost of implementing these plans was to be assessed directly on consumers.⁸ From July 2011 through December 2012, AB 2398 required that manufacturers assess consumers a charge of five cents (\$0.05) per square yard.⁹ Thereafter, the amount of the assessment could be increased to “be sufficient to meet, but not exceed, the anticipated costs of carrying out the plan.”¹⁰

AB 2398 recognized CARE as the sole approved carpet stewardship organization through April 1, 2015. CARE’s initial, five-year California stewardship plan was approved by CalRecycle in January 2012. CARE remains the sole such approved organization.

Collected fees are distributed by CARE as incentive payments and subsidies to increase the diversion and recycling rates and as grants and loans. Substantial funds also are spent on education and other activities.

However, in 2014, the price of oil—the raw material for virgin synthetic carpet fiber—plunged. One result was the reduction in demand for recycled fiber. As a result, the subsidies available from CARE were insufficient to support continued investment in the construction or even the operation of recycling capacity.

The diversion and recycling rates declined and have not quickly recovered, even though the consumer fee was increased to \$0.10 and then \$0.20.

The recently rejected 2017-2022 plan proposes to increase the per-yard consumer assessment again, to \$0.25. It also includes a number of other new steps intended to encourage increased diversion and output of recycled material in what remains a very difficult economic situation. But the magnitude of the challenge is substantial. The demand for synthetic carpet floor coverings is not inelastic, and the magnitude of the fee—especially for large-scale purchasers—is having an impact on carpet sales. For example, according to testimony at CalRecycle’s December 20 hearing on the 2017-2022 plan, at current prices of carpet to property developers, a \$0.25 fee would increase flooring costs by 5% to 6%, thus encouraging developers and property

owners to switch to other floor coverings.¹¹ And even though the actual dollar increase on smaller jobs is less substantial, consumers still are switching away from carpet: the proportion of carpet to other floor covering sales at one retailer who testified on December 20 has declined from 90% to 29%.¹²

Recent Action

CARE’s initial plan was to run until December 31, 2016. In October 2016, after repeated skirmishes with CalRecycle about the adequacy of its ongoing existing plan (more on that later), CARE submitted its proposed 2017-2021 plan. It was published for comment and subject to a public hearing on December 20.

Shortly before the hearing, CalRecycle released a staff memorandum that identified two options for action on the CARE submission.¹³ One was to approve it. The second was to disapprove it, require submission of a new plan within 60 days, and allow another 60 days for finalization of that plan before any enforcement action was taken.

The staff report included seven findings as to the proposed plan’s inadequacy. Some are relatively minor, and do not seem likely to be insurmountable impediments to developing an acceptable final plan. For example, the staff criticized the plan for not discussing how stakeholder input is to be evaluated and acted upon, and its failure to identify or evaluate education and outreach activities.

But others are much more fundamental to the future feasibility of the program. These go to the sufficiency of funds that would result from increasing the per-year consumer fee per square yard of carpet to \$0.25 to “support[] a nascent California carpet recycling industry struggling to stay in business.”¹⁴ The staff also criticized the plan for not addressing “the possibility of providing subsidies” at various points in the supply chain, such as to installers or to carpet manufacturers who use recovered fiber; failure to provide payments to underwrite equipment for better identification of resin content; and failure to include “other ideas to improve the market mechanisms in the Program.”¹⁵

CalRecycle staff did not dispute that the price of oil has dramatically impacted this program. The staff report concedes that “CARE rightly notes markets for many recyclables, including [post-consumer carpet] have been extremely challenging in recent years.”¹⁶ Rather than discussing how that demand decline affects the feasibility of a carpet recycling program, however, the staff concluded that “it is all the more imperative for CARE to closely monitor financial incentives and be prepared to offset loss of value in down periods.”¹⁷

Indeed, the staff report is replete with implications that cost is no object—for example, that “the 2017 plan does not sufficiently address the critical role of calibrating market-based financial mechanisms to overcome material price fluctuations and stabilize recycling investments over the long term.”¹⁸ The closest the staff report came to addressing economic feasibility is to state its view that “while PRC § 42973 required CalRecycle to find the assessment ‘will not create an unfair advantage in the market place for one or more companies in the organization . . .’ before approving a Plan, preserving serving carpet’s share of the overall flooring market relative to other flooring types is not a goal of AB 2398.”¹⁹

At the December 20 hearing, Director Smithline pointed out that, notwithstanding the economics of recycling, he was obliged to comply with the legislature’s mandate. But he seemed to focus principally on the statutory goal of “increasing the landfill diversion and recycling of postconsumer carpet generated in California” and requirements that a program “incentivize the market growth of secondary products made from postconsumer carpet,”²⁰ and that program operators “demonstrate to the department that it has achieved continuous meaningful improvement in the rates of recycling and diversion”²¹ He did not appear to give any attention to the implications of the statute’s “feasibility” requirements.

And on December 22, Director Smithline chose the staff’s second recommended option—rejection of the plan but deferral of enforcement for up to 120 days while plan revisions were considered and developed.

What Next?

As CARE, the carpet industry more broadly, and individual manufacturers whose products currently are being sold in California, consider the options in response to the December 22 decision, the potential for both enforcement action and legislative changes merits recognition.

First, AB 2398 requires that carpet manufacturers submit acceptable stewardship plans to CalRecycle²² and prohibits (among other things) any “manufacturer, wholesaler or retailer” from offering carpet for sale in California if the carpet is not subject to an approved plan.²³ It also authorizes civil penalties of up to \$10,000 per day for violations.²⁴

Moreover, enforcement is not a concern only as to industry’s response to the Director’s December 22 decision. As signaled above, CalRecycle also made public in December a memorandum from its enforcement branch as to the “Status of the Enforcement Evaluation of CARE’s 2015 Annual Report.”²⁵ This memo presents a response to a September 20, 2016, directive from the CalRecycle Director that the Waste Evaluation and Enforcement Branch evaluate potential enforcement actions arising from CARE’s pre-2016 annual reports.

The enforcement memo recommends that “pursuing civil penalties (in coordination with the legal office) . . . on CARE is the most appropriate course of action at this time.”²⁶ That recommendation is based upon finds that “Program goals are not showing continuous meaningful improvement,” consumers “do not have reasonable access to recycling services in all counties,” education efforts have not adequately increased recycling or diversion, and “CARE is not responding to market changes in a timely manner with assessment and incentive adjustments, and the assessment may not be set high enough to fund infrastructure development and drive markets for increased recycled output.”²⁷

In short, neither CARE nor the companies it is serving can have confidence that, even as they work to accommodate the concerns expressed in the disapproval of the 2017-2021 plan in a timely way, CARE will not face penalty actions. CalRecycle has raised the stakes.

Second, the CalRecycle staff memorandum that recommended denial of the new plan curiously contains a section captioned “Possible Changes to Statute.” In it, the staff “suggests that specific additions are needed to strengthen the original carpet statute and provide CalRecycle, as the oversight agency, with additional

flexibility to assist a program that is under-performing and out of compliance to come back into compliance (beyond the use of assessing penalties).²⁸ Among the “high level *concepts*” the staff identified are establishment of rates and dates mandates, giving CalRecycle authority to prescribe specific actions to be taken by a stewardship organization (such as requiring all grant funds to go to California businesses or organizations), establishing minimum-recycled content requirements for new carpet, and tougher enforcement authorities.²⁹

Given the near-absolute control of the California government by Democrats, and that party’s historic inclinations as to stewardship programs, it is hard to see this section as anything less than another shot over the bow to encourage industry to make the current system work as CalRecycle would prefer.

There can be little doubt that, as this article is going to press, carpet manufacturers, wholesalers, and retailers doing business in California, or supplying carpet to those who do so, are considering their options. Presumably, by late February the future direction of carpet recycling efforts in the state will become more clear. In the meantime, other businesses facing product stewardship challenges would be well advised to be cautious before endorsing “visible fee” programs, and to pay close attention to the details of any statutes or ordinances that propose to do so.

¹ Chapter 20 of California’s Public Resources Code, Cal. Pub. Res. Code §§ 42970, et seq.

² 2010 Cal. Legis. Serv. Ch. 681 (A.B. 2398) § 1(f) (emphasis added).

³ Cal. Pub. Res. Code § 42972(a)(2).

⁴ *Id.* § 42972(a)(3).

⁵ *Id.* § 42972(a)(5).

⁶ *Id.* § 42975(a) (emphasis added).

⁷ *Id.* § 42972(a)(6)(c)(2) (initial plan) (emphasis added); *Id.* § 42973(a)(2)(B) (plans after April 1, 2015).

⁸ *Id.* § 42972.5.

⁹ *Id.* § 42972(a).

¹⁰ *Id.* § 42972 (a) (6)(c)(2).

¹¹ Department of Resources Recycling and Recovery (CalRecycle) Monthly Public Meeting (Dec. 20, 2016) (Statement of Robert Peoples, Executive Director of CARE).

¹² *Id.* (Statement of Larry Slick).

¹³ Memorandum from Howard Levenson to Scott Smithline re Consideration for Approval of California Carpet Stewardship.

¹⁴ *Id.* at 3.

¹⁵ *Id.* at 4.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.* at 6.

¹⁹ *Id.* at 4.

²⁰ 2010 Cal. Legis. Serv. Ch. 681 (A.B. 2398) § 1(f).

²¹ Cal. Pub. Res. Code § 42975(a).

²² *Id.* § 42972(a).

²³ *Id.* § 42974.

²⁴ *Id.* § 42978.

²⁵ Memorandum from Mark Debie to Scott Smithline re status of the Enforcement of CARE’s 2015 Annual Report (Dec. 20, 2016).

²⁶ *Id.* at 1.

²⁷ *Id.* at 3.

²⁸ Levenson, *supra* note 13 at 16.

²⁹ *Id.* at 16-7 (emphasis in original).